SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1951

No. 559

THE UNITED STATES, PETITIONER,

vs.

BELL AIRCRAFT CORPORATION.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS.

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1 IN THE COURT OF CLAIMS OF THE UNITED STATES

No. 47745

BELL AIRCRAFT CORPORATION, *Plaintiff*,

v.

THE UNITED STATES OF AMERICA, *Defendant*.

PETITION.

Filed July 7, 1947

To The Honorable the Chief Justice and Associate Justices of the Court of Claims of the United States.

FIRST CAUSE OF ACTION.

For its First Cause of Action plaintiff states:

1. Plaintiff is a corporation organized and existing under the laws of the State of New York with its principal office and place of business in the Town of Wheatfield, Niagara County, New York.

2. Plaintiff was organized and commenced business in 1935 and thereafter, during all the times mentioned herein, the major part of plaintiff's business has been the development and manufacture of military aircraft.

2 3. On August 14, 1941, plaintiff entered into Contract No. W535 ac-20910 with the defendant represented by Ennis McCall, First Lieutenant, United States Army Air Corps, Contracting Officer, whereby plaintiff undertook to furnish and deliver to the defendant certain military aircraft, more fully described in said contract, in consideration of defendant's agreement to reimburse plaintiff in full for the cost of manufacturing said aircraft and in addition to pay plaintiff a fixed fee, said contract being generally known as, and hereinafter referred to as, a cost-plus-a-fixed-fee contract. A copy of the pertinent parts of said contract is attached hereto marked Exhibit A. Certain terms of the contract were altered from time to time by change orders and supplemental agreements, none of which is pertinent to this suit, except

the termination settlement agreement hereinafter referred to. The said contract was terminated by the defendant for its convenience on August 14, 1945, and thereafter, under date of December 21, 1945, plaintiff and defendant entered into a settlement agreement pursuant to the Contract Settlement Act of 1944, wherein the rights and liabilities of the parties under said contract were settled and determined, except the rights and liabilities with respect to certain excepted claims, including the claim alleged in this first cause of action.

4. Plaintiff, in accordance with the terms of said contract, furnished defendant with the military aircraft required by the said contract to be furnished by plaintiff to defendant and duly performed all the conditions required by it by said contract.

5. Defendant accepted the military aircraft furnished by plaintiff pursuant to said contract.

3 6. In the years 1938, 1939 and 1940, plaintiff performed three experimental fixed price contracts for the United States Government for the manufacture and delivery of certain experimental military airplanes known as Model XFN 1 (the "Airacuda"), Model XP 39 (the "Airacobra"), and Model XFL 1 (the "Airabonita"). One experimental airplane was manufactured under each contract. In the development of the three experimental airplanes, plaintiff expended for experimental and development work, the sum of $1,499,739.23 over and above the total contract price for the three airplanes. This amount was set up in a deferred experimental and development account for future amortization. The Company has amortized this deferred experimental and development cost over all airplanes which have been manufactured by it since the performance of the aforedescribed experimental contracts which have included principles of design developed in the performance of said experimental contracts.

7. The airplanes manufactured under Contract No. W535 ac-20910 incorporated principles of design developed in the performance of the aforedescribed experimental contracts.

8. Under the terms of Contract No. W535 ac-20910 plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performin the contract the sum of $370,552.30, which is the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. W535 ac-20910 up to and including August 31, 1943. Plaintiff alleges that the experimental and development costs included in said

vouchers were reimbursable costs of performing the said contract.

4 9. In 1940, plaintiff commenced a greatly expanded tooling program to enable it to produce the airplanes called for by contracts then in process of negotiation and to meet the production requirements of anticipated future contracts. During the years of 1940 and 1941, plaintiff expended the sum of $1,874,725.77 in said tooling program. This amount was set up in the deferred experimental and development account described in paragraph 6 to be amortized over future production. The tooling acquired in the course of this program was used in the production of all P-39 airplanes produced by plaintiff, and upon the termination of plaintiff's contracts for said P-39 airplanes in the years 1944 and 1945, was treated by the defendant as its property and was disposed of as defendant's property pursuant to defendant's instructions.

10. The plaintiff has amortized said tooling costs over all airplanes on which the tooling acquired, as aforesaid, was used.

11. Under the terms of Contract No. W535 ac-20910, plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract, the sum of $819,571.64. This amount represented the portion of said tooling costs allocable to the airplanes manufactured under Contract No. W535 ac-20910 up to and including August 31, 1943. Plaintiff alleges that the tooling costs included in said vouchers were reimbursable costs of performing the said contract.

12. The defendant's contracting officer, pursuant to the authority vested in him by the terms of said contract, duly determined that the said amount of $1,190,123.94, the total amount of
5 deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. W535 ac-20910 up to and including August 31, 1943, were reimbursable costs of performing said contract under the terms thereof, and plaintiff was reimbursed for them. Thereafter, the General Accounting Office erroneously determined that said costs were not so reimbursable and defendant recouped said amount by deducting the same from sums otherwise due and owing the plaintiff from the defendant.

13. Under the terms of Contract No. W535 ac-20910, plaintiff also submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract the sum of $194,947.81, representing the portion of said amortized experimental and

development costs allocable to the airplanes manufactured under Contract No. W535 ac-20910 subsequent to August 31, 1943, and the sum of $79,991.20 representing the portion of said tooling costs similarly allocable.

14. The defendant has refused to pay plaintiff the amount of $274,939.01, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. W535 ac-20910 subsequent to August 31, 1943, and claimed by plaintiff as a reimbursable cost for performing said contract.

15. The administrative action taken by defendant in connection with plaintiff's claim is as follows:

(a) From 1940 to 1942, plaintiff amortized the entire amount of said experimental and development and tooling costs over airplanes produced under fixed price contracts then on hand. In 1942, at which time defendant was performing Contract
6 No. W535 ac-20910 and other cost-plus-fixed-fee contracts for military aircraft, the defendant, acting through the Treasury Department, determined that said experimental, development and tooling costs should be allocated to the airplanes produced under Contract No. W535 ac-20910 and other cost-plus-fixed-fee contracts, as well as the fixed price contracts performed by plaintiff in 1940, 1941 and 1942. It therefore, disallowed $2,286,819.95 of the experimental, development and tooling costs as a business expense allocable to the performance of fixed price contracts in the years 1940, 1941 and 1942, and provided for the amortization of this amount to the airplanes produced under Contract No. W535 ac-20910 and other cost-plus-fixed-fee contracts. Plaintiff paid an income tax on the increased income in the years 1941 and 1942 resulting from the disallowance of $2,286,819.95 as business expense allocable to the production of the airplanes produced under the fixed price contracts performed by the plaintiff during those years.

(b) The Secretary of War acting through the War Department Price Adjustment Board, renegotiated the profits plaintiff made under said fixed fee contracts, and in determining the amount of plaintiff's profits subject to renegotiation and the portion thereof which represented excessive profits under the Renegotiation Act of 1942, as amended, disallowed as costs under said fixed price contracts the same amount of experimental, development and tooling costs which had been allocated to said fixed price contracts as the Treasury dis-

7 allowed and entered into a written agreement that the costs so disallowed on fixed price contracts would become items of reimbursable cost under plaintiff's cost-plus-fixed-fee contracts and would be allowed and reimbursed as such. Contract No. W535 ac-20910 is one of such cost-plus-fixed-fee contracts. Said written agreement is attached hereto and marked Exhibit B.

(c) As hereinbefore alleged, plaintiff submitted vouchers in the amount of $274,939.01 for reimbursement of experimental, development and tooling costs allocable to airplanes produced under Contract No. W535 ac-20910 subsequent to August 31, 1943. The contracting officer decided by written decision, dated March 1, 1945, that plaintiff was not entitled to reimbursement for said costs. Plaintiff duly appealed from this determination to the Secretary of War. The said appeal was heard and considered by the War Department Board of Contract Appeals, as the representative of the Secretary of War and the said Board affirmed the contracting officer's determination by decision dated April 29, 1946. Plaintiff's application to said Board for a rehearing was denied by the Board's order dated May 31, 1946. The administrative action taken with respect to the aforesaid $1,190,123.94 of experimental, development and tooling costs allocable to said contract during the period up to and including August 31, 1943, is set forth in paragraph 12 above.

16. The plaintiff is justly entitled to recover from the defendant the sum of $274,939.01 on account of experimental,
8 development and tooling costs allocable to Contract No. W535 ac-20910 subsequent to August 31, 1943, and the sum of $1,190,123.94 on account of such costs allocable to said contract up to and including August 31, 1943.

17. Plaintiff is sole and absolute owner of the claim herein presented, has made no transfer or assignment of the said claim or any part thereof, or any interest therein, and is justly entitled to the amount claimed herein from the United States, after allowing all just credits and off-sets. Plaintiff has at all times borne true allegiance to the Government of the United States and has not in any way aided, abetted or given encouragement to rebellion against the United States and believes the facts stated in this petition to be true.

SECOND CAUSE OF ACTION.

18. Plaintiff incorporates herein by reference the allegations contained in paragraphs 1 and 2 of its First Cause of Action.

19. On September 10, 1941, plaintiff entered into Contract No. DA-W535 ac-156 with the defendant represented by R. H. Wheat, Major, United States Army Air Corps, Contracting Officer, whereby plaintiff undertook to furnish and deliver to the defendant certain military aircraft, more fully described in said contract, in consideration of defendant's agreement to reimburse plaintiff in full for the cost of manufacturing said aircraft and in addition to pay plaintiff a fixed fee, said contract being generally known as, and hereinafter referred to as a cost-plus-a-fixed-fee contract.

A copy of the pertinent parts of said contract is attached hereto and marked Exhibit C. Certain terms of the contract were
9 altered from time to time by change orders and supplemental agreements, none of which is pertinent to this suit.

20. Plaintiff incorporates herein by reference the allegations contained in paragraphs 4, 5 and 6 of its first cause of action.

21. The airplanes manufactured under Contract No. DA-W535 ac-156 incorporated principles of design developed in the performance of the aforedescribed experimental contracts.

22. Under the terms of Contract No. DA-W535 ac-156 plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract the sum of $37,318.96, which is the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. DA-W535 ac-156 up to and including August 31, 1943. Plaintiff alleges that the experimental and development costs included in said vouchers were reimbursable costs of performing the said contract.

23. In 1940, plaintiff commenced a greatly expanded tooling program to enable it to produce the airplanes called for by contracts then in process of negotiation and to meet the production requirements of anticipated future contracts. During the years of 1940 and 1941, plaintiff expended the sum of $1,874,725.77 in said tooling program. This amount was set up in the deferred experimental and development account described in paragraph 6 of the "First Cause of Action" to be amortized over future production. The tooling acquired in the course of this program was used in the Production of all P-39 airplanes produced by plaintiff, and upon the termination of plaintiff's contracts for said P-39 air-
10 planes in the years 1944 and 1945, was treated by the de-

fendant as its property and was disposed of as defendant's property pursuant to defendant's instructions.

24. The plaintiff has amortized said tooling costs over all airplanes on which the tooling acquired, as aforesaid, was used.

25. Under the terms of Contract No. DA-W535 ac-156, plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract, the sum of $72,413.12. This amount represented the portion of said tooling costs allocable to the airplanes manufactured under Contract No. DA-W535 ac-156 up to and including August 31, 1943. Plaintiff alleges that the tooling costs included in said vouchers were reimbursable costs of performing the said contract.

26. The defendant's contracting officer, pursuant to the authority vested in him by the terms of said contract, duly determined that the said amount of $109,732.08, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. DA-W535 ac-156 up to and including August 31, 1943, were reimbursable costs of performing said contract under the terms thereof, and plaintiff was reimbursed for them. Thereafter, the General Accounting Office erroneously determined that said costs were not so reimbursable and defendant recouped said amount by deducting the same from sums otherwise due and owing the plaintiff from the defendant.

27. Under the terms of Contract No. DA-W535 ac-156, plaintiff also submitted to defendant cost vouchers which included as
11 a reimbursable cost of performing the contract the sum of $13,888.85, representing the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. DA-W535 ac-156 subsequent to August 31, 1943, and the sum of $4,371.50 representing the portions of said tooling costs similarly allocable.

28. The defendant has refused to pay the plaintiff the amount of $18,260.35, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. DA-W535 ac-156 subsequent to August 31, 1943, and claimed by plaintiff as a reimbursable cost of performing said contract.

29. The administrative action taken by defendant in connection with plaintiff's claim is as follows:

(a) From 1940 to 1942, plaintiff amortized the entire amount of said experimental, development and tooling costs over air-

planes produced under fixed price contract then on hand. In 1942, at which time defendant was performing Contract No. DA-W535 ac-156 and other cost-plus-fixed-fee contracts for military aircraft, the defendant, acting through the Treasury Department, determined that said experimental, development and tooling costs should be allocated to the airplanes produced under Contract No. DA-W535 ac-156 and other cost-plus-fixed-fee contracts, as well as the fixed price contracts performed by plaintiff in 1940, 1941 and 1942. It, therefore, disallowed $2,286,819.95 of the experimental development and tooling costs as a business expense allocable
12 to the performance of fixed price contracts in the years 1940, 1941 and 1942, and provided for the amortization of this amount to the airplanes produced under Contract No. DA-W535 ac-156 and other cost-plus-a-fixed-fee contracts. Plaintiff paid an income tax on the increased income in the years 1941 and 1942 resulting from the disallowance of $2,286,819.95 as business expense allocable to the production of the airplanes produced under the fixed price contracts performed by the plaintiff during those years.

(b) The Secretary of War acting through the War Department Price Adjustment Board, renegotiated the profits plaintiff made under said fixed fee contracts, and in determining the amount of plaintiff's profits subject to renegotiation and the portion thereof which represented excessive profits under the Renegotiation Act of 1942, as amended, disallowed as costs under said fixed price contracts the same amount of experimental, development and tooling costs which had been allocated to said fixed price contracts as the Treasury disallowed and entered into a written agreement that the costs so disallowed on fixed price contracts would become items of reimbursable cost under plaintiff's cost-plus-fixed-fee contracts and would be allowed and reimbursed as such. Contract No. DA-W535 ac-156 is one of such cost-plus-fixed-fee contracts. Said written agreement is attached hereto and marked Exhibit B.

(c) As hereinbefore alleged, plaintiff submitted vouchers in the amount of $18,260.35 for reimbursement of experimental, de-
13 velopment and tooling costs allocable to airplanes produced under Contract No. DA-W535 ac-156 subsequent to August 31, 1943. The contracting officer decided by written decision, dated March 1, 1945, that plaintiff was not entitled to reimbursement for said costs. Plaintiff duly appealed from this determination to the Secretary of War. The said ap-

peal was heard and considered by the War Department Board of Contract Appeals, which reported its decision affirming the decision of the Contracting Officer to the President of said Board as the authorized representative of the Secretary of War, whose decision was in accord therewith. Plaintiff's application to said Board for a rehearing was denied by the Board's order dated May 31, 1946. The administrative action taken with respect to th.. aforesaid $109,732.08 of experimental, development and tooling costs allocable to said contract during the period up to and including August 31, 1943, is set forth in paragraph 26 above.

30. The plaintiff is justly entitled to recover from the defendant the sum of $18,260.35 on account of experimental, development and tooling costs allocable to Contract No. DA-W535 ac-156 subsequent to August 31, 1943, and the sum of $109,732.08 on account of such costs allocable to said contract up to and including August 31, 1943.

31. Plaintiff is sole and absolute owner of the claim herein presented, has made no transfer or assignment of the said claim or any part thereof, or any interest therein, and is justly entitled to the amount claimed herein from the United States, after allowing all just credits and offsets. Plaintiff has at all times borne true allegiance to the Government of the United States and has not in any way aided, abetted, or given encouragement to rebellion against the United States and believes the facts stated in this petition to be true.

14

THIRD CAUSE OF ACTION.

32. Plaintiff incorporates herein by reference the allegations contained in paragraphs 1 and 2 of its first cause of action.

33. On June 29, 1942, plaintiff entered into Contract No. W535 ac-29318 with the defendant represented by Joseph E. Derham, Lieutenant Colonel, United States Army Air Forces, Contracting Officer, whereby plaintiff undertook to furnish and deliver to the defendant certain military aircraft, more fully described in said contract, in consideration of defendant's agreement to reimburse plaintiff in full for the cost of manufacturing said aircraft and in addition to pay plaintiff a fixed fee, said contract being generally referred to as a cost-plus-a-fixed-fee contract. A copy of the pertinent parts of said contract is attached hereto and marked Exhibit D. Certain terms of the contract were altered from time to time by change orders and supplemental agreements, of which the following are pertinent to this suit:

(1) Supplemental Agreement No. 2, dated September 29, 1942, whereby the model airplane to be furnished was changed from Army Air Forces Model P-39-E to Model P-63A-1;

(2) Supplemental Agreement No. 37, dated April 13, 1945, whereby Contract No. W535 ac-40041 to which a portion of
15 said costs were originally allocable, was combined with and merged into Contract W535 ac-29318.

(3) Supplemental Agreement No. 64, dated May 15, 1946, which is the termination settlement agreement referred to below.

The said contract was terminated by the defendant for its convenience on August 14, 1945, and thereafter, under date of May 15, 1946, plaintiff and defendant entered into a settlement agreement, pursuant to the Contract Settlement Act of 1944, whereby the rights and liabilities of the parties under said contract were settled and determined, except the rights and liabilities with respect to certain excepted items, including the claim alleged in this third cause of action.

34. Plaintiff, in accordance with the terms of said contract, furnished defendant with the military aircraft required by the said contract to be furnished by plaintiff to defendant and duly performed all the conditions required of it by said contract.

35. Defendant accepted the military aircraft furnished by plaintiff pursuant to said contract.

36. In the years 1938, 1939 and 1940, plaintiff performed three experimental fixed price contracts for the United States Government for the manufacture and delivery of certain experimental military airplanes known as Model XFN 1 (the "Airacuda"), Model XP 39 (the "Airacobra"), and Model XFL 1 (the "Airabonita"). One experimental airplane was manufactured under each contract. In the development of the three experimental airplanes, plaintiff expended for experimental and development work, the sum of $1,499,739.23 over and above a total contract
16 price for the three airplanes. This amount was set up in a deferred experimental and development account for future amortization. The Company has amortized this deferred experimental and development cost over all airplanes which have been manufactured by it since the performance of the aforedescribed experimental contracts which have included principles of design developed in the performance of said experimental contracts.

37. The airplanes manufactured under Contract No. W535 ac-29318 incorporated principles of design developed in the performance of the aforedescribed experimental contracts.

38. Under the terms of Contract W535 ac-29318 plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract the sum of $223,288.09, which is the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. W535 ac-29318 subsequent to August 31, 1943. Plaintiff alleges that the experimental and development costs included in said vouchers were reimbursable costs of performing the said contract.

39. In 1940, plaintiff commenced a greatly expanded tooling program to enable it to produce the airplanes called for by contracts then in process of negotiation and to meet the production requirements of anticipated future contracts. During the years of 1940 and 1941, plaintiff expended the sum of $1,874,725.77 in said tooling program. This amount was set up in the deferred experimental and development account described in paragraph 6 of the First Cause of Action to be amortized over future production. The tooling acquired in the course of this program was used in
17 the production of all P-39 airplanes produced by plaintiff, and upon the termination of paintiff's contracts for said P-39 airplanes in the years 1944 and 1945, was treated by the defendant as its property and was disposed of as defendant's property pursuant to defendant's instructions.

40. The plaintiff has amortized said tooling costs over all airplanes on which tooling acquired, as aforesaid, was used.

41. Under the terms of Contract No. W535 ac-29318, plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract, the sum of $69,895.04. This amount represented the portion of said tooling costs allocable to the airplanes manufactured under Contract No. W535 ac-29318 subsequent to August 31, 1943. Plaintiff alleges that the tooling costs included in said vouchers were reimbursable costs of performing the said contract.

42. The defendant has refused to pay plaintiff the amount of $293,183.13, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. W535 ac-29318 subsequent to August 31, 1943, and claimed by plaintiff as a reimbursable cost for performing said contract.

43. The administrative action taken by defendant in connection with plaintiff's claim is as follows:

(a) From 1940 to 1942, plaintiff amortized the entire amount of said experimental, development and tooling costs over

airplanes produced under fixed price contracts then on hand. In 1942, at which time defendant was performing Contract
18 No. W535 ac-29318 and other cost-plus-fixed-fee contracts for military aircraft, the defendant, acting through the Treasury Department, determined that said experimental, development and tooling costs should be allocated to the airplanes produced under Contract No. W535 ac-29318 and other cost-plus-fixed-fee contracts, as well as the fixed price contracts performed by plaintiff in 1940, 1941 and 1942. It, therefore, disallowed $2,286,819.95 of the experimental, development and tooling costs as a business expense allocable to the performance of fixed price contracts in the years 1940, 1941 and 1942, and provided for the amortization of this amount to the airplanes produced under Contract No. W535 ac-29318 and other cost-plus-a-fixed-fee contracts. Plaintiff paid an income tax on the increased income in the years 1941 and 1942 resulting from the disallowance of $2,286,819.95 as business expense allocable to the production of the airplanes produced under the fixed price contracts performed by the plaintiff during those years.

(b) The Secretary of War acting through the War Department Price Adjustment Board, renegotiated the profits plaintiff made under said fixed fee contracts, and in determining the amount of plaintiff's profits subject to renegotiation and the portion thereof which represented excessive profits under the Renegotiation Act of 1942, as amended, disallowed as costs under said fixed price contracts the same amount of experimental, development and tooling costs which had been allocated to said fixed price contracts as the Treasury
19 disallowed and entered into a written agreement that the costs so disallowed on fixed price contracts would become items of reimbursable cost under plaintiff's cost-plus-fixed-fee contracts and would be allowed and reimbursed as such. Contract No. W535 ac-29318 is one of such cost-plus-fixed-fee contracts. Said written agreement is attached hereto and marked Exhibit B.

(c) As hereinbefore alleged, plaintiff submitted vouchers in the amount of $293,183.13 for reimbursement of experimental, development and tooling costs allocable to airplanes produced under Contract No. W535 ac-29318 subsequent to August 31, 1943. The contracting officer decided by written decision, dated March 1, 1945, that the plaintiff was not entitled to reimbursement for said costs. Plaintiff duly appealed from this determination to the Secretary of War.

The said appeal was heard and considered by the War Department Board of Contract Appeals as, the representative of the Secretary of War, and the said Board affirmed the contracting officer's determination by decision dated April 29, 1946. Plaintiff's application to said Board for a rehearing was denied by the Board's order dated May 31, 1946.

44. The plaintiff is justly entitled to recover from the defendant the sum of $293,183.13 on account of experimental, development and tooling costs allocable to Contract No. W535 ac-29318.

45. Plaintiff is sole and absolute owner of the claim herein presented, has made no transfer or assignment of the said
20 claim or any part thereof, or any interest therein, and is justly entitled to the amount claimed herein from the United States, after allowing all just credits and offsets. Plaintiff has at all times borne true allegiance to the Government of the United States and has not in any way aided, abetted, or given encouragement to rebellion against the United States and believes the facts stated in this petition to be true.

FOURTH CAUSE OF ACTION.

46. Plaintiff incorporates herein by reference the allegations contained in paragraphs 1 and 2 of its first cause of action.

47. On September 28, 1943, plaintiff entered into Contract W535 ac-40071 with the defendant represented by Robert A. Watson, Captain, United States Air Corps, Contracting Officer, whereby plaintiff undertook to furnish and deliver to the defendant certain military aircraft, more fully described in said contract, in consideration of defendant's agreement to reimburse plaintiff in full for the cost of manufacturing said aircraft and in addition to pay plaintiff a fixed fee, said contract being generally referred to as a cost-plus-a-fixed-fee contract. A copy of the pertinent parts of said contract is attached hereto and marked Exhibit E. Certain terms of the contract were altered from time to time by change orders and supplemental agreements, of which the following are pertinent to this suit; (1) Change Order No. 3 dated December 24, 1943, a copy of the pertinent part of which is included in Exhibit E; (2) Supplemental Agreement No. 36, dated February 22, 1946, which is the termination settlement agreement referred to below.

21 The said contract was terminated by the defendant for its convenience on August 14, 1945, and thereafter under

date of February 22, 1946, plaintiff and defendant entered into a settlement agreement pursuant to the Contract Settlement Act of 1944, whereby the rights and liabilities of the parties under said contract were settled and determined, except the rights and liabilities with respect to certain excepted items, including the claim alleged in this Fourth Cause of Action.

48. Plaintiff, in accordance with the terms of said contract, furnished defendant with the military aircraft required by the said contract to be furnished by plaintiff to defendant and duly performed all the conditions required of it by said contract.

49. Defendant accepted the military aircraft furnished by plaintiff pursuant to said contract.

50. In the years 1938, 1939 and 1940, plaintiff performed three experimental fixed price contracts for the United States Government for the manufacture and delivery of certain experimental military airplanes known as Model XFN 1 (the "Airacuda"), Model XP 39 (the "Airacobra"), and Model XFL 1 (the "Airabonita"). One experimental airplane was manufactured under each contract. In the development of the three experimental airplanes, plaintiff expended for experimental and development work, the sum of $1,499,739.23 over and above a total contract price for three airplanes. This amount was set up in a deferred experimental and development account for future amortization. The Company has amortized this deferred experimental and development cost over all airplanes which have been manufactured
22 by it since the performance of the aforedescribed experimental contracts which have included principles of design developed in the performance of said experimental contracts.

51. The airplanes manufactured under Contract No. W535 ac-40071 incorporated principles of design developed in the performance of the aforedescribed experimental contracts.

52. Under the terms of Contract No. W535 ac-40071 plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract the sum of $195,922.72, which is the portion of said amortized experimental and development costs allocable to the airplanes manufactured under Contract No. W535 ac-40071 subsequent to August 31, 1943. Plaintiff alleges that the experimental and development costs included in said vouchers were reimbursable costs of performing the said contract.

53. In 1940, plaintiff commenced a greatly expanded tooling program to enable it to produce the airplanes called for by contracts then in process of negotiation and to meet the production

requirements of anticipated future contracts. During the years of 1940 and 1941, plaintiff expended the sum of $1,874,725.77 in said tooling program. This amount was set up in the deferred experimental and development account described in paragraph 6 of the First Cause of Action to be amortized over future production. The tooling acquired in the course of this program was used in the production of all P-39 airplanes produced by plaintiff, and upon the termination of plaintiff's contracts for said P-39 airplanes in the years 1944 and 1945, was treated by the defendant as
23 its property and was disposed of as defendant's property pursuant to defendant's instructions.

54. The plaintiff has amortized said tooling costs over all airplanes on which the tooling acquired, as aforesaid, was used.

55. Under the terms of Contract No. W535 ac-40071, plaintiff submitted to defendant cost vouchers which included as a reimbursable cost of performing the contract, the sum of $204,658.72. This amount represented the portion of said tooling costs allocable to the airplanes manufactured under Contract No. W535 ac-40071 subsequent to August 31, 1943. Plaintiff alleges that the tooling costs included in said vouchers were reimbursable costs of performing the said contract.

56. The defendant has refused to pay plaintiff the amount of $400,581.44, the total amount of deferred experimental, development and tooling costs allocated to the airplanes manufactured under Contract No. W535 ac-40071 subsequent to August 31, 1943, and claimed by plaintiff as a reimbursable cost for performing said contract.

57. The administrative action taken by defendant in connection with plaintiff's claim is as follows:

(a) From 1940 to 1942, plaintiff amortized the entire amount of said experimental, development and tooling costs over airplanes produced under fixed price contracts then on hand. In 1942, at which time defendant was performing Contract No. W535 ac-40071 and other cost-plus-fixed-fee contracts for military aircraft, the defendant, acting through the
24 Treasury Department, determined that said experimental, development and tooling costs should be allocated to the airplanes produced under Contract No. W535 ac-40071 and other cost-plus-fixed-fee contracts, as well as the fixed price contracts performed by plaintiff in 1940, 1941 and 1942. It, therefore, disallowed $2,286,819.95 of the experimental, development and tooling costs as a business expense allo-

cable to the performance of fixed priced contracts in the years 1940, 1941 and 1942, and provided for the amortization of this amount to the airplanes produced under Contract No. W535 ac-40071 and other cost-plus-a-fixed-fee contracts. Plaintiff paid an income tax on the increased income in the years 1941 and 1942 resulting from the disallowance of $2,286,819.95 as business expense allocable to the production of the airplanes produced under the fixed contracts performed by the plaintiff during those years.

(b) The Secretary of War acting through the War Department Price Adjustment Board, renegotiated the profits plaintiff made under said fixed fee contracts, and in determining the amount of plaintiff's profits subject to renegotiation and the portion thereof which represented excessive profits under the Renegotiation Act of 1942, as amended, disallowed as costs under said fixed price contracts the same amount of experimental, development and tooling costs which had been allocated to said fixed price contracts as the Treasury disallowed and entered into a written agreement that the costs so disallowed on fixed price contracts would become items of reimbursable cost under plaintiff's cost-plus-fixed-fee contracts and would be allowed and reimbursed as such. Contract No. W535 ac-40071 is one of such cost-plus-fixed-fee contracts. Said written agreement is attached hereto and marked Exhibit B.

(c) As hereinbefore alleged, plaintiff submitted vouchers in the amount of $400,581.44 for reimbursement of experimental, development and tooling costs allocable to airplanes produced under Contract No. W535 ac-40071 subsequent to August 31, 1943. The contracting officer decided by written decision, dated March 1, 1945, that plaintiff was not entitled to reimbursement for said costs. Plaintiff duly appealed from this determination to the Secretary of War. The said appeal was heard and considered by the War Department Board of Contract Appeals, as the representative of the Secretary of War, and the said Board affirmed the contracting officer's determination by decision dated April 29, 1946. Plaintiff's application to said Board for a rehearing was denied by the Board's order dated May 31, 1946.

58. The plaintiff is justly entitled to recover from the defendant the sum of $400,581.44 on account of experimental, development

and tooling costs allocable to Contract No. W535 ac-40071 subsequent to August 31, 1943.

59. Plaintiff is sole and absolute owner of the claim herein presented, has made no transfer or assignment of the said claim or any part thereof, or any interest therein, and is justly entitled to the amount claimed herein from the United States, after allowing all just credits and off-sets. Plaintiff has at all times borne true allegiance to the Government of the United States and has not in any way aided, abetted, or given encouragement to rebellion against the United States and believes the facts stated in this petition to be true.

WHEREFORE, plaintiff prays judgment against the United States on the four causes of action contained in this petition in the sum of $2,286,819.95.

DUDLEY, STOWE & SAWYER,
Attorneys for
Bell Aircraft Corporation,
Manufacturers & Traders Building,
Buffalo, New York

COVINGTON, BURLING, RUBLEE,
ACHESON & SHORB,
Union Trust Building,
Washington, D. C.
Of Counsel.

Exhibit A to Petition

Pertinent portions of Contract No. W535 ac-20910

ARTICLE 1—*Statement of Work*

(a) The Contract shall, within the time specified in Article 4 hereof, manufacture, furnish and deliver to the Government the following articles:

Item (1)—Eighteen Hundred (1800) Airplanes, Interceptor Pursuit, Single-Place, Single-Engine, Contractor's type and Model 15, being known and designated as Air Corps' Type and Model P-39-D, as completed and manufactured in accordance with Bell Aircraft Corporation Model Specification No. 4Y003J, dated July 30, 1941, hereby made a part hereof.

(This article contains additional provisions for the furnishing of spare parts and technical data which are omitted)

ARTICLE 3—*Consideration*

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in the contract, subject to reimbursement for cost as outlined in Article 6 hereof, the cost, plus a fixed fee of Four Million Two Hundred Fifty-Seven Thousand Six Hundred Forty Four Dollars and Forty Cents ($4,257,644.40) being six percent of the total estimated cost of Seventy Million Nine Hundred Sixty Thousand and Seven Hundred Forty Dollars ($70,960,740.00). This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of the fixed-fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost.

29 (b) For the purpose of determining the amount payable under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. It being understood and agreed without limiting the generality of the foregoing that

(1) All costs which have been incurred by the Contractor in anticipation of this contract and prior to the signing thereof, and which if incurred after the signing of this contract, would have been considered as allowable items of cost within the meaning of said regulations, shall be considered as allowable items of cost incurred hereunder.

(2) Any cost incurred by the Contractor under the terms of this Contract which would constitute an allowable item of cost under the provisions of paragraph (b) of this article shall be included in determining the amount payable under this contract, notwithstanding any provision contained in the specifications or other documents incorporated in this contract by reference, designating services to be performed or materials to be furnished by the Contractor at its expense or without cost to the Government.

In the event that prior to final settlement under this contract such regulations be amended so as to provide for additional allowable items of cost such additional items shall be considered allowable items hereunder.

(c) The Contractor shall, to the extent of his ability, procure materials and services at the most advantageous prices available with due regard to securing prompt delivery of satisfactory materials, take all cash and trade discounts, rebates, allowances, credits, salvage, commissions and bonifications, and when unable to take advantage of such benefits he shall promptly notify the Contracting Officer to that effect and the reason therefor. In determining the actual net cost of articles and materials of every kind required for the purpose of this contract, there shall be deducted from the gross cost thereof all cash and trade discounts, rebates, allowances, credits, salvage, commissions and bonifications which have accrued to the benefit of the Contractor or would have so accrued except for the fault or neglect of the Contractor. Such benefits lost through no fault or neglect on the part of the Contractor, or lost through fault of the Government, shall not be deducted from gross costs.

ARTICLE 6—*Payments*

(a) *Reimbursement for Cost.* The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 as may be approved or ratified and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers. Provided, however, that subject to the requirement of paragraph (c) of Article 7 hereof, in respect of the maintenance so far as practicable of a complete separate system of accounts for work under this contract, in the event it be impracticable to furnish the Contracting Officer with original signed payrolls for labor, original paid invoices for materials, or other original papers, the Contractor shall furnish evidence in a form satisfactory to the Contracting Officer, covering expenditures to be reimbursed under this article. Generally, reimbursement will be made weekly but may be made at more frequent intervals if the conditions so warrant.

ARTICLE 16—*Disputes*

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his

decision to writing and mail a copy thereof to the Con-
31 tractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. The Contractor shall be afforded an opportunity to be heard and offer evidence in support of his appeal. The president of the board, from time to time, may divide the board into divisions of one or more members and assign members thereto. A majority of the members of the board or of a division thereof shall constitute a quorum for the transaction of the business of the board or of a division, respectively, and the decision of a majority of the members of the board or of a division shall be deemed to be the decision of the board or of a division, as the case may be. If a majority of the members of a division are unable to agree on a decision or if within 30 days after a decision by a division, the board or the president thereof directs that the decision of the division be reviewed by the board, the decision will be so reviewed, otherwise the decision of a majority of the members of a division shall become the decision of the board. If a majority of the members of the board is unable to agree upon a decision, the president will promptly submit the appeal to the Under Secretary of War for his decision upon the record. A vacancy in the board or in any division thereof shall not impair the powers nor affect the duties of the board or division nor of the remaining members of the board or division, respectively. Any member of the board, or any examiner designated by the president of the board for that purpose, may hold hearings, examine witnesses, receive evidence and report the evidence to the board or to the appropriate division, if the case is pending before a division. Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum
or sums allowed to the Contractor under the provisions of
32 this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

EXHIBIT B TO PETITION.

September 7, 1943

Price Adjustment Board
War Department, I T & T Building
67 Broad Street
New York, New York

Dear Sirs:

Attention: Major Knox B. Phagan

Pursuant to our telephone conversation this afternoon, we should be glad if you would indicate your approval of the method to be followed in amortizing development and experimental expenses and production tooling costs of P-39 airplanes.

Our records as of December 31, 1942 and the schedules originally submitted to you showed that we had amortized the full amount of these costs against fixed price contracts. You objected to such treatment on the ground that the costs should be amortized over cost plus a fixed fee as well as fixed price contracts. The Bureau of Internal Revenue in examining our Federal income and excess profits tax return for the calendar year 1941 had made the same objection and required us to amortize the costs over all airplane contracts then held by us. In view of the position taken by the Bureau of Internal Revenue and yourselves we have agreed to amortize the experimental and development expenditures over all contracts for P-39 and P-63 airplanes and the P-39 production tooling expenditures over all contracts for P-39 airplanes, provided that, the amounts disallowed by you against fixed price contracts become items of reimbursable costs under our cost plus a fixed fee contracts and are allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office. Under date of August 14, 1943 we
33 provided you with two schedules which set forth in detail the amounts and contracts involved in the writeoff from January 1, 1940 to June 30, 1943 on an actual writeoff basis and through the balance of 1943 and 1944 on an estimated basis.

The method agreed upon involved a determination of each of the two amounts involved, which amounts are as shown by our books (and less adjustments aggregating $2,892.19 are as shown by a report of an Agent of the Bureau of Internal Revenue as of December 31, 1940) less adjustments made by the Contract Audit Section of the Army Air Forces as a result of their examination of their costs. The amounts are as follows:

Price Adjustment Board
Attention: Major Knox B. Phagan

September 8, 1943.

	Development and Experimental	P-39 Production Tooling	Together
Costs to December 31, 1940 (there were no additions subsequently)	$1,528,760.66	$1,894,109.57	$3,422,870.23
Less—Costs disallowed by Contract Audit Section, Army Air Forces	29,021.43	19,383.80	48,405.23
Amount to be amortized as agreed upon with Price Adjustment Board and Contract Audit Section, Army Air Forces	$1,499,739.23	$1,874,725.77	$3,374,465.00

The last amounts shown above are to be amortized over all fixed price and cost plus a fixed fee supply contracts for P-39 and P-63 airplanes as follows:

The sum of the number of airplanes and equivalents on order and undelivered at the beginning of the year and the number of airplanes and equivalents ordered during the calendar year is to be divided into the unamortized costs as of the beginning of the year, the resulting quotient represents the amortization per airplane. The amortization per airplane
34 multiplied by the number of airplanes and equivalents accepted by the Army Air Forces during the period of each contract results in the amortization per contract.

We believe the foregoing sets the understanding between us as to the amortization of the expenditures for exprimental and development and P-39 production tooling and if it is in accordance with your understanding we should like you to so indicate by signing one copy of this letter and returning it to us.

Yours very truly,

BELL AIRCRAFT CORPORATION
JOHN BERRY, JR. /s/
JOHN BERRY, JR.
Comptroller

JB,Jr:rla

The explanation and method of amortization set forth in this letter is in accordance with our understanding and has our approval.

Signed: KNOX B. PHAGAN
Major A. C.
Price Adj. Officer
Date: Sept. 9, 43

EXHIBIT C TO PETITION.

Pertinent portions of Contract No. DA-W535 ac-156

ARTICLE 1—*Statement of Work*

(a) The Contractor shall, within the time specified in Article 4 hereof, manufacture, furnish and deliver to the Government the following articles:

Item 1—Two Hundred (200) Airplanes, Pursuit, Single-Place, Single-Engine, Contractor's type and Model 14, being known and designated as Air Corps Model P-39D-1, as constructed in accordance with Bell Aircraft Corporation Specification No. 14-945-001-1 dated May 20, 1941, packed for overseas shipment.

Item 2—One Hundred Forty-Four (144) Airplanes Pursuit, Single-Place, Single-Engine, Contractor's type and Model 14, being known and designated as Air Corps Model P-39D-1, as constructed in accordance with Bell Aircraft Corporation Specification No. 14-945-001-1, dated May 20, 1941, set up and serviced for fly-away at Contractor's flying field.

(Additional provisions covering the furnishing of spare parts and data are omitted)

ARTICLE 3—*Consideration*

(a) The Government will pay the contractor upon satisfactory delivery of all items specified in the contract, subject to reimbursement for costs as outlined in Article 6 hereof, the cost, plus a fixed fee of Eight Hundred Ninety-Nine Thousand One Hundred Fifty-Five and 56/100 Dollars ($899,155.56), being Six percent of the total estimated cost of Fourteen Million Nine Hundred Eighty Five Thousand Nine Hundred Twenty-Six dollars ($14,985,926.00). This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost.

(b) For the purpose of determining the amount payable under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with regulations for determination of the cost of performing a contract as promulgated by the

Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. It being
36 understood and agreed without limiting the generality of the foregoing that:

(1) All costs which have been incurred by the Contractor in anticipation of this contract and prior to the signing thereof, and which if incurred after the signing of this contract would have been considered as allowable items of cost within the meaning of this article shall be allowable items of cost hereunder;

(2) Any cost incurred by the Contractor under the terms of this contract which would constitute an allowable item of cost under the provisions of paragraph (b) of this article shall be included in determining the amount payable under this contract notwithstanding any provisions contained in the specifications or other documents incorporated in this contract by reference, designating services to be performed or materials to be furnished by the Contractor at its expense without cost to the Government.

(c) In the event that prior to final settlement under this contract, the above-mentioned regulations (T. D. 5000) shall have been amended either on or before the effective date of this contract so as to provide for additional allowable items of cost, such additional items shall be considered allowable items hereof.

ARTICLE 6—*Payments*

(a) *Reimbursement for Cost.* The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 as may be approved or ratified and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers. Provided, however, that subject to the requirement of paragraph (c) of Article 7 hereof, in respect of the maintenance so far as practicable of a complete separate system of accounts for work under this contract, in the event it be impracticable to furnish the Contracting Officer
37 with original signed payrolls for labor, original paid invoices for materials, or other original papers, the Contractor shall furnish evidence in a form satisfactory to the Contracting Officer, covering expenditures to be reimbursed under this article. Generally, reimbursement will be made weekly but may be made at more frequent intervals if the conditions so warrant.

ARTICLE 16—*Disputes*

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the Contracting Officer, subject to written appeal by the Contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties hereto. In the meantime the Contractor shall diligently proceed with performance.

EXHIBIT D TO PETITION.

Pertinent portions of Contract No. W535 ac-29318

ARTICLE 1—*Statement of Work*

(a) The Contractor shall, within the time specified in Article 4 hereof, manufacture, furnish and deliver to the Government the following articles:

Item 1—Two Thousand (2000) airplanes, Intereceptor Pursuit, single place, single engine, Contractor's Type and Model 28, Air Corps Type and Model P-39-E, each complete and conforming to Contractor's Specification No. 28-947-001, dated January 14, 1942, hereby made a part hereof.
(This article contains additional provisions for the furnishing of spare parts and technical data which are omitted)

ARTICLE 3—*Consideration*

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in this contract, subject to
38 reimbursements for cost, as outlined in Article (6) hereof, the cost, plus a fixed fee of Three Million Five Hundred Forty-six Thousand Eight Hundred Dollars and no cents ($3,546,800.00) being four per cent (4%) of the total estimated cost of Eighty-eight Million Six Hundred Seventy Thousand Dollars and no cents ($88,670,000.00). This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof; provided, however, that there shall be no adjustment in the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation because of any errors and/or omissions made in computing the original estimated cost or where the estimated cost varies from the actual cost.

(b) For purposes of determining the amounts payable to the Contractor under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with regulations for the determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter I of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War, August 2, 1940, it being understood and agreed, without limiting the generality of the foregoing, that:

(1) All costs which have been incurred by the Contractor in anticipation of this contract and prior to the signing thereof, and which if incurred after the signing of this contract would have been considered as allowable items of cost within the meaning of this article, shall be allowable items of cost hereunder.

(2) Interest on unreimbursed portions of actual investments in a facility or facilities used for the performance of this contract and acquired pursuant to any Emergency Plant Facilities Contract or Contracts with the Government, now in effect or hereafter entered into, including any amendment thereof, at the rate or rates provided for in the Emergency
39 Plant Facilities Contract or Contracts involved shall be an allowable cost hereunder to the extent that such interest accrues during the performance of this contract; provided, that if the facility or facilities also are used concurrently for the perfomance of another contract or contracts, only so much of such interest as is proportionate to the use of the facility or facilities for the performance of this contract shall be an allowable cost hereunder; and, provided further, that such interest shall not be an allowable cost hereunder to the extent that such interest is allowed as a cost under any other contract or contracts.

(3) Cost of such bonds and insurance as the Contracting Officer may approve or require and cost and expenses incurred in the defense and/or discharge of such claims of others on account of death or bodily injury of persons or loss or destruction of or damage to property as may arise out of or in connection with the performance of the work under this contract shall be an allowable item of cost hereunder, provided that such reimbursement shall not include any amount for which the Contractor is indemnified or compensated by insurance or otherwise, or any amount for which it would have been so indemnified or compensated except for the failure of the Contractor to procure or maintain bonds

or insurance in accordance with the requirements of the Contracting Officer. The foregoing shall not restrict the right of the Contractor to be reimbursed for the cost of insurance covering the Contractor's property or property for which the Contractor is responsible to someone other than the Government and which is used or to be used in the performance of this contract.

ARTICLE 6—*Payments*

a) *Reimbursement for Cost.*—The Government will currently reimburse the Contractor for such expenditures made in ac-
40 cordance with Article 3 hereof as may be approved or ratified by the Contracting Officer, and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers; provided, however, that subject to the requirement of paragraph (b) of Article 7 hereof, in respect of the maintenance so far as practicable of a complete separate system of accounts for work under this contract, in the event in be impracticable to furnish the Contracting Officer with original signed payrolls for labor, original paid invoices for materials, or other original papers, the Contractor shall furnish evidence in a form satisfactory to the Contracting Officer, covering expenditures to be reimbursed under this Article. Generally, reimbursement will be made weekly, but may be made at more frequent intervals if the conditions so warrant.

ARTICLE 9—*Termination of Contract by Government.*

(b) Upon the termination of this contract as hereinbefore provided, full and complete settlement of all claims of the Contractor arising out of this contract shall be made as follows:

(3)(a) The Government shall reimburse the Contractor for such further expenditures after the date of termination, if approved by the Contracting Officer as necessarily expended or incurred by the Contractor, as would, if incurred before such termination, have been considered as allowable items of cost within the meaning of T. D. 5000. To the extent that the Contracting Officer may find such further costs to have been necessarily expended or incurred by the Contractor, it is understood and agreed without limiting the generality of the foregoing that such further necessary expenditures may include rental charges during the period while Government property remains in the possession of the Contractor, wages of employees from the date of termination to the earliest date of layoff consistent with Collector's established pro-
41 cedure, separation payments to employees on account of

layoffs required by such termination made in accordance with collective bargaining contracts between the Contractor and the recognized representatives of its employees, deferred development costs, direct expense, general overhead expense and the cost of tools, jigs, dies, patterns, templates and fixtures not theretofore charged to the cost of sales, the costs of cancellation of subcontracts and purchase orders, and claims arising therefrom, the costs of storage, packing, transportation and delivery to the Government of Government property, and such other expenditures as the Contracting Officer may approve.

ARTICLE 16—*Disputes*

(Added by Supplemental Agreement No. 2, dated September 29, 1942)

Except as otherwise specifically provided in this contract all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. The Contractor shall be afforded an opportunity to be heard and offer evidence in support of his appeal. The president of the board, from time to time, may divide the board into divisions of one or more members and assign members thereto. A majority of the members of the board or of a division thereof shall constitute a quorum for the transaction of the business of the board or
42 of a division, respectively, and the decision of a majority of the members of the board or of a division shall be deemed to be the decision of the board or of a division, as the case may be. If a majority of the members of a division are unable to agree on a decision or if within 30 days after a decision by a division, the board or the president thereof directs that the decision of the division be reviewed by the board, the decision will be so reviewed, otherwise the decision of a majority of the members of a division shall become the decision of the board. If a majority of the members of the board is unable to agree upon a decision, the president will promptly submit the appeal to the Under Secretary of War for his decision upon the record. A vacancy in the board or in any

division thereof shall not impair the powers nor affect the duties of the board or division nor of the remaining members of the board or division, respectively. Any member of the board, or any examiner designated by the president of the board for that purpose, may hold hearings, examine witnesses, receive evidence and report the evidence to the board or to the appropriate division, if the case is pending before a division. Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

Whenever in any other Article of this Contract any reference is made to Article 16, such reference shall be deemed to be to the foregoing provisions of this Article.

43

EXHIBIT E TO PETITION. t

Pertinent Portions of Contract No. W535 ac-40071

ARTICLE 1—*Statement of Work*

The Contractor shall, within the time specified in Article 4 hereof, manufacture, furnish and deliver to the Government the following articles:

Item 1—Two Thousand (2,000) Airplanes, Fighter, Single Engine, Single Place, Contractor's Type and Model 26E series, Army Air Forces Type and Model P-39Q Series, Each complete and conforming to Contractor's Specification No. 4Y003J-Q10 dated 24 April 1943, hereby made a part hereof.
(This article contains additional provisions for the furnishing of spare parts and technical data which are omitted.)

ARTICLE 3—*Consideration*

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in this contract, subject to reimbursements for cost, as outlined in Article (6) hereof, the cost, plus a fixed fee of Two Million Seven Hundred Thirty-five Thousand Four Hundred Eighty-eight Dollars and No Cents ($2,735,488.00) being four per cent (4%) of the total estimated cost of Sixty-eight Million Three Hundred Eighty-seven Thousand Two

Hundred Dollars and No Cents ($68,387,200.00) as set forth in Article 2. This estimated cost and the fixed fee are subject to increases or decreases as provided herein. There shall be no adjustment in the amount of the fixed fee, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost or because of the fact that the estimated cost varies from the actual cost.

44 (b) For the purposes of determining the amounts payable to the Contractor under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with regulations for the determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter I of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War, August 2, 1940, it being understood and agreed, without limiting the generality of the foregoing, that:

(1) All costs which have been incurred by the Contractor in anticipation of this contract and prior to the signing thereof, and which if incurred after the signing of this contract would have been considered as allowable items of cost within the meaning of this Article, shall be allowable items of cost hereunder.

(2) Interest on unreimbursed portions of actual investments in a facility or facilities used for the performance of this contract and acquired pursuant to any Emergency Plant Facilities Contract or Contracts with the Government, now in effect or hereafter entered into, including any amendment thereof, at the rate or rates provided for in the Emergency Plant Facilities Contract or Contracts involved, shall be an allowable cost hereunder to the extent that such interest accrues during the performance of this contract; provided, that if the facility or facilities also are used concurrently for the performance of another contract or contracts, only so much of such interest as is proportionate to the use of the facility or facilities for the performance of this contract shall be an allowable cost hereunder; and, provided further, that such interest shall not be an allowable cost hereunder to the extent that such interest is allowed as a cost under any other contract or contracts.

45 (3) Cost of such bonds and insurance as the Contracting Officer may approve or require and cost and expenses incurred in the defense and/or discharge of such claims of others on account of death or bodily injury of persons or

loss or destruction of or damage to property as may arise out of or in connection with the performance of the work under this contract shall be an allowable item of cost hereunder, provided that such reimbursement shall not include any amount for which the Contractor is indemnified or compensated by insurance or otherwise, or any amount for which it would have been so indemnified or compensated except for the failure of the Contractor to procure or maintain bonds or insurance in accordance with the requirements of the Contracting Officer. The foregoing shall not restrict the right of the Contractor to be reimbursed for the cost of reasonable insurance covering the Contractor's property or property for which the Contractor is responsible to someone other than the Government and which is used or to be used in the performance of this contract.

ARTICLE 6—*Payments*

(a) *Reimbursement for Cost.*—The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 hereof as may be approved or ratified by the Contracting Officer, and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers; provided, however, that subject to the requirement of paragraph (b) of Article 7 hereof, in respect of the maintenance so far as practicable of a complete separate system of accounts for work under this contract, in the event it be impracticable to furnish the Contracting Officer with original signed payrolls for labor, original paid invoices for materials, or other original papers, the Contractor shall furnish evidence in a form satisfactory to the Con-
46 tracting Officer, covering expenditures to be reimbursed under this Article. Generally, reimbursement will be made weekly, but may be made at more frequent intervals if the conditions so warrant.

ARTICLE 9—*Termination of Contract by Government.*

(b) Upon the termination of this contract as hereinbefore provided, full and complete settlement of all claims of the Contractor arising out of this contract shall be made as follows:

(3) (a) The Government shall reimburse the Contractor for such further expenditures after the date of termination, if approved by the Contracting Officer as necessarily expended or incurred by the Contractor, as would, if incurred before such termination, have been considered as allowable items of cost within the meaning of

T. D. 5000. To the extent that the Contracting Officer may find such further costs to have been necessarily expended or incurred by the Contractor, it is understood and agreed without limiting the generality of the foregoing that such further necessary expenditures may include rental charges during the period while Government property remains in the possession of the Contractor, wages of employees from the date of termination to the earliest date of layoff consistent with the Contractor's established procedure, separation payments to employees on account of layoffs required by such termination made in accordance with collective bargaining contracts between the Contractor and the recognized representatives of its employees, deferred development costs, direct expense, general overhead expense and the cost of tools, jigs, dies, sales, the cost of cancellation of subcontracts and purchase orders, and claims arising therefrom, the costs of storage, packing, transportation and delivery to the Government of Government property, and such other expenditures as the Contracting Officer may approve.

The foregoing excerpt from Article 9(b) was amended by Change Order No. 3 dated December 17, 1943, to read as follows:

47 "(a) The Government shall reimburse the Contractor for such further expenditures after the date of termination, if approved by the Contracting Officer as necessarily expended or incurred by the Contractor as would if incurred before such termination, have been considered as allowable items of cost within the meaning of T. D. 5000. To the extent that the Contracting Officer may find such further costs to have been necessarily expended or incurred by the Contractor, it is understood and agreed without limiting the generality of the foregoing that such further necessary expenditures may include rental charges during the period while Government property remains in the possession of the Contractor, wages of employees from the date of termination to the earliest date of layoff consistent with Contractor's established procedure, separation payments to employees on account of layoffs required by such termination made in accordance with collective bargaining contracts between the Contractor and the recognized representatives of its employees, deferred development costs, direct expense, general overhead expense, and the cost of tools, jigs, dies, patterns, templates and fixtures not theretofore charged to the cost of sales, the cost of cancellation of subcontracts and purchase orders, and claims arising therefrom, the costs of storage, packing, transportation and delivery to the Government of Government property, and such other expenditures as the Contracting Officer may approve."

REASON: To correct a typographical error.

ARTICLE 16—*Disputes*

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto.

48 The Secretary of War may, in his discretion, designate an individual, or individuals other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. The Contractor shall be afforded an opportunity to be heard and offer evidence in support of his appeal. The president of the board, from time to time, may divide the board into divisions of one or more members and assign members thereto. A majority of the members of the board or of a division thereof shall constitute a quorum for the transaction of the business of the board or of a division, respectively, and the decision of a majority of the members of the board or of a division shall be deemed to be the decision of the board or of a division, as the case may be. If a majority of the members of a division are unable to agree on a decision or if within 30 days after a decision by a division, the board or president thereof directs that the decision of the division be reviewed by the board, the decision will be so reviewed, otherwise the decision of a majority of the members of a division shall become the decision of the board. If a majority of the members of the board is unable to agree upon a decision, the president will promptly submit the appeal to the Under Secretary of War for his decision upon the record. A vacancy in the board or in any division thereof shall not impair the powers nor affect the duties of the board or division nor of the remaining members of the board or division, respectively. Any member of the board, or any examiner designated by the president of the board for that purpose, may hold hearings, examine witnesses, receive evidence and report the evidence to the board or to the appropriate division, if the case is pending before a division. Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

49 **GENERAL TRAVERSE—Filed Aug. 18, 1947.**

And now comes the Attorney General, on behalf of the United States, and answering the petition of the claimant herein, denies each and every allegation therein contained; and asks judgment that the petition be dismissed.

/s/ HERBERT A. BERGSON
Acting Assistant Attorney General.

JBM
HAB

51 IN THE UNITED STATES COURT OF CLAIMS

No. 47745

Filed May 18, 1950

BELL AIRCRAFT CORPORATION

v.

THE UNITED STATES

REPORT OF COMMISSIONER—Filed May 18, 1950

To the Honorable the CHIEF JUDGE AND ASSOCIATE JUDGES OF THE UNITED STATES COURT OF CLAIMS:

Pursuant to the order of reference in the above-entitled case, the undersigned commissioner herewith makes the following report of his findings of fact:

1. The plaintiff is a corporation organized and existing under the laws of the State of New York with its principal office and place of business in the Town of Wheatfield, Niagara County, New York.

2. The plaintiff was organized and commenced business in 1935, and thereafter, during all the times mentioned herein, the major part of the plaintiff's business has been the development and manufacture of military aircraft.

EXPERIMENTAL AND DEVELOPMENT COSTS DEFERRED

3. In 1936, 1937, and 1938, the plaintiff entered into certain experimental contracts with the defendant, through the United States Army Air Corps for the construction of certain experimental and service test airplanes. Experimental airplanes were designated by the letter "X" preceding the model number, and the service test airplanes were designated by the letter "Y" preceding the model number. Other designations of type preceding the model number of particular airplanes hereinafter mentioned were "F" for "Fighter" and "P" for "Pursuit."

52 4. The following fixed-price experimental contracts were entered into between the plaintiff and the United States for fighter planes, in the performance of which the plaintiff incurred substantial expenditures over and above amounts received, which costs were set up on the plaintiff's books as deferred charges applicable to anticipated future production:

Item	Date of contract	Contract numbers	Airplanes Units	Models	Designations	Contract price
(A)	5/12/36	W 535 ac-8773	1	XFM-1	"Airacuda"	$ 390,000
(B)	9/27/37	W 535 ac-10341 ...	1	XP-39	"Airacobra"	245,000
(C)	4/20/38	W 535 ac-11122 ...	10	YFM-1	"Airacuda"	3,168,350
			3	YFM-1A		
(D)	11/ 8/38	63629	1	XFL-1	"Airabonita"	245,000
			16			4,049,446

The foregoing contracts are referred to in paragraphs 3 to 6, inclusive, of the stipulation between counsel (Plaintiff's Exhibit 1) and designated as Exhibits A to D, inclusive, to such stipulation. They are incorporated herein by reference. Contract No. 63629 was with the Navy, Bureau of Supplies and Accounts, and the others were with the Army Air Corps.

Articles 19, 21, 27, and 29, respectively, of the foregoing contracts provide for a nonexclusive, irrevocable right and license to the Government to use any and all discoveries, inventions, improvements and/or suggestions which are wholly or in part developed, perfected and/or reduced to practice with the aid and/or cooperation of the Government or of Government personnel, and/or by the contractor to meet explicit Governmental requirements or by the fulfillment of such contract.

Articles 26, 26 and 25, respectively, of the Army contracts provide:

> ***Reproduction rights.***—It is understood and agreed that the contractor does not convey to the Government any reproduction rights in or to the articles and/or spare parts called for herein by virtue of the terms of this contract, except as hereinbefore set forth.

53 The plaintiff acquired a number of basic patents in connection with its development work, on which substantial royalties were realized.

5. All the airplanes delivered on these experimental contracts, as well as the production contracts received later, were powered by liquid-cooled Allison engines, furnished by the Government. The Government also furnished other materials and parts, consisting of the wheels, tires, tubes, propellers, guns, instruments and certain electrical and communications equipment.

The Airacuda was a twin-engine, five-place, long-range fighter plane with pusher propellers operated by drive shafts to the engine. It was armed with two 37mm. repeating cannon, flexibly mounted in the nose of its engine nacelles, and two 50-calibre machine guns installed in the waist, with flexible mountings manually

operated, with a wide sweep firing range upward, downward or rearward. These planes were originally designed with conventional landing gear, that is, with two wheels abreast under each wing and a tail wheel to carry the rear portion of the fuselage. The three YFM-1A service test model Airacudas incorporated the tricycle landing gear which had been developed in connection with the experimental Airacobra.

The Allison engines supplied for the experimental planes operated at maximum power at sea level. The plaintiff installed an external General Electric turbo supercharger, driven from the engine, which increased its power at high altitudes. Allison later delivered altitude-rated engines, which duplicated the external unit and voided its further use. Two of the service test Airacudas incorporated the altitude-rated engines. The Airacuda was approximately two and one-half times the weight of the Airacobra.

The Airacobra was a single-engine and propeller, single-seat, short-range interceptor fighter plane. The engine, mounted to the rear of the cockpit, operated the propeller at the nose of the plane by means of a drive shaft. A tricycle landing gear was developed in the experimental model which consisted of a retractable nose wheel and two retractable wing wheels. The Airacobra was armed
with one 37mm. repeating cannon which fired through the
54 shaft and hub of the propeller from a fixed mounting, and
two 50-calibre machine guns which fired from fixed mountings between the propeller blades, so that the position of the plane governed the aim at a target, without any manual control.

The Airabonita was modeled after the Airacobra, but adapted to use on airplane carriers. The conventional landing gear was restored to this model and a tail hook was provided to engage the carrier deck arresting gear for landing purposes.

6. The first experimental Airacuda had been substantially completed by the end of 1937, and the excess of costs over the contract price for this unit was charged to profit and loss accounts for that year. Subsequent to the delivery of this airplane in 1938, the plaintiff incurred additional expenditures for the development and improvement in this design. The plaintiff's expenditures for the 13 test models of this design were also substantially in excess of the contract price received. These excess costs were capitalized as "deferred charges" in 1939 and 1940 for distribution as an element of cost against future production.

Much of the basic engineering and development designing in the Airacuda was carried forward and incorporated in the Airacobra which later entered quantity production for the Army Air Corps and the British Government.

The tooling for experimental contract work was of a temporary nature and fixtures for assembly were made of wood, very little of

which had any useful value for later production. All excess costs on experimental contracts were classified as experimental and development expense. Such costs were accumulated from year to year during the performance of the several experimental contracts. No segregation of these costs was made as to their application to the specific contracts on which excessive costs were incurred, except the first amount deferred in 1938, which resulted from work on the experimental contract for the Airacobra.

The plaintiff deferred and capitalized experimental and development costs as follows:

December 31, 1938	$ 128,052.77
December 31, 1939	511,776.21
December 31, 1940	888,931.68
Total	1,528,760.66

55 Although the deferred experimental and development costs were not segregated in the plaintiff's accounts in respect to the specific contracts under which excess costs were incurred, the plaintiff's auditors reported approximate allocations as follows:

Airacudas	$ 889,499.48
Airacobra	229,086.30
Airabonita	410,174.88
Total	1,528,760.66

The defendant's Army Audit Agency disallowed items totaling $29,021.43, leaving a balance of $1,499,739.23 in the deferred account for experimental and development expense, which sum represented the plaintiff's costs over and above the sums received under the contracts for experimental airplanes.

7. The plaintiff received no production contracts for any of the types described as Airacudas or the Airabonita airplanes. It received many contracts for great numbers of the Airacobra pursuit fighter plane, known as the P–39.

PRODUCTION TOOLING COSTS DEFERRED

8. On April 26, 1939, the plaintiff entered into contract W 535 ac–12635 with the Army Air Corps for the delivery of 13 service test models of the Airacobra with additional parts at a fixed price of $1,073,445. Twelve of these planes were described as YP–39, Model 4–C, and one YP–39A, Model 4–D.

The work under this contract was merged in the shop with production on later contracts, and any additional experimental costs in connection with its performance were absorbed in the production costs on fixed-price production contracts.

Thereafter, from time to time, the plaintiff was awarded additional production contracts for P–39 Airacobras with both the United States and the British Governments. The earlier production contracts were fixed price, and the later ones were cost-plus-fixed-fee contracts. Under the cost-plus-fixed-fee contracts, hereinafter referred to as CPFF contracts, the plaintiff was reimbursed for allowable costs of manufacture and was paid a fixed fee specified in the contract.

56 The production of P–39 Airacobras was continued on all of these contracts until April 1944, at which time the uncompleted contracts were amended to provide for deliveries of P–63 models. Numerous changes were made during the entire production period of the P–39 models to reduce costs and facilitate production, to avoid field breakage and to improve functional operations.

9. The plaintiff received the following fixed-price contracts for the production and delivery of Airacobra fighter planes:

Item	Date of contract	Contract numbers	Unit planes and equivalent in spare parts	Models	Contract price
United States					
(E)	4/26/39	W 535 ac-12635	13 1	YP-39 YP-39A	$1,073,445.00
(F)	9/30/39	W 535 ac-13383	87	P-39C	2,833,236.00
(G)	9/ 7/40	W 535 ac-15675 Increased	120 565	P-39D	4,962,220.00 21,276,912.79
(H)	6/ 5/41	W 535 ac-32	180	P-39D-1	7,407,540.00
			966		37,553,353.79
British					
	8/15/40	A-218	200	P-400	9,517,507.55
	10/ 8/40	A-1326	250	P-400	9,647,163.33
	10/10/40	A-1476	360	P-400	14,645,980.19
Totals			810		33,810,651.07
			1,776		71,364,004.86

The foregoing contracts are referred to in paragraphs 8 to 14, inclusive, of the stipulation of facts. The United States contracts were entered into with the Army Air Corps, copies of which are designated as Exhibits E to H to the stipulation and incorporated herein by reference.

The Model P–400 produced under British contracts was the British version of the P–39 and was of similar type and character as the Airacobra pursuit fighter planes specified under the contracts with the United States Army Air Corps.

The Army Air Corps contracts contain similar provisions, in respect to the right and license of the Government in any and
57 all discoveries, inventions and improvements, as those set

forth in Finding 4 for experimental contracts. These contracts also contain provisions substantially as follows:

> *Provisions Reference Section 14 of the Act Approved April 3, 1939—Limitation on Profits—It is expressly understood and agreed by both parties hereto that the contractor hereby agrees:*
>
> • • • • •
>
> (e) That the manufacturing spaces and books of its own plant, affiliates, and subdivisions shall at all times be subject to inspection and audit by any person designated by the Secretary of War, the Secretary of the Treasury and/or by a duly authorized committee of Congress.
>
> • • • • •
>
> *Cost Records.*—The contractor agrees to keep cost records in accordance with its own methods and practices of computing costs of all expenses incurred by it in connection with the performance of this contract and such records shall be available for inspection of the Contracting Officer or his representative after the completion or earlier termination of this contract. Such cost data shall be for the information of the Government, but shall in no way affect the contract price of the articles, spare parts, supplies or work covered by this contract.

10. About April 1939, when the plaintiff received its contract for the production of service test models of the P–39 Airacobra, it began to fabricate and install permanent tooling for the production of this type of airplane. Production tooling is distinguished from ordinary machine tools, in that the latter are more permanent and universal in character, consisting of milling machines, lathes, drill presses, etc., not restricted in use to specific models or types of the product manufactured.

Production tooling for the P–39 pursuit fighter plane was largely assembly tooling, consisting of long-beam assembly, subassembly and tail-assembly fixtures, all of which were fabricated in structural steel and remained in use as long as this type of plane was in production. It also included metal tubes, angles, form blocks, jigs, router templets and templet dies. In the production of ex-
58 perimental models, most of these fixtures were fabricated in wood, and tooling was provided for temporary use. But, in the production of service planes the plaintiff was required to provide for interchangeability of certain parts, such as wings, tails, and surface landing gear, necessitating accurate duplications of the various parts.

As additional contracts for Airacobras were received during 1939 and 1940, the plaintiff increased its numbers of assemblies to provide for greater production and duplicated the tooling for such assemblies, subassemblies, and such auxiliary tooling as became necessary to meet increased production requirements. The plaintiff provided tooling for its Niagara Falls plant, which started operations in June 1941, similar to that it had installed in its Elmwood Avenue plant.

During 1939 and 1940, the plaintiff incurred costs for production tooling for the P–39 Airacobra in the sum of $1,894,109.57. In December 1940, the plaintiff recorded this sum in a deferred account, together with the deferred costs on experimental contracts, entitled "Experimental, Development and Production Tooling Expenses." The defendant's Army Audit Agency disallowed $19,383.80 of the deferred cost for tooling, leaving $1,874,725.77 for allocation to future production.

11. In addition to the special production tooling set forth in the preceding finding, a substantial amount of additional tooling was required in the fabrication of P–39 airplanes. In connection with the plaintiff's quotations on each of the fixed-price contracts, except the last two British contracts, the plaintiff submitted a breakdown of its estimated costs of production. These cost estimates contained no provision for the amortization of any part of the deferred experimental, development and production tooling costs.

A substantial portion of the experimental expense and production tooling costs had not been determined or set up in the deferred account at the times the plaintiff submitted its estimates of production costs for fixed-price contracts which it received during 1939 and 1940.

The plaintiff's estimated tool charges for the various fixed-price contracts, other than the deferred costs, totaled $2,597,435.40. Its actual tooling costs for fixed-price production, other than the deferred tooling, were $2,233,239.47.

59 Some of the tools which had been provided as a preliminary to production and deferred for allocation against future production, would become worn out by use or obsolete as a result of current changes in design. Some were reworked and others were scrapped and replaced. The costs of reworking or replacing original tooling would be charged against current production and would be included in the tool costs in the preceding paragraph.

AMORTIZATION OF EXPERIMENTAL, DEVELOPMENT AND PRODUCTION TOOLING EXPENSE

12. As of December 31, 1940, the plaintiff had capitalized and deferred experimental, development and production tooling expense, as follows:

	Amounts expended and deferred by plaintiff	Disallowed by Army Audit	Net amounts subject to amortization
Experimental and development expense (Finding 6)	$1,528,760.66	$29,021.43	$1,499,739.23
Production tooling for P-39's (Finding 10)	1,894,109.57	19,383.80	1,874,725.77
Total	3,422,870.23	48,405.23	3,374,465.00

13. The plaintiff originally planned to amortize its deferred costs of $3,374,464 or the basis of the number of planes delivered and to be delivered on all contracts on hand at the end of each year, and by prorating such costs annually against deliveries made during the current year.

A copy of the memorandum by Paul C. Gillette, Engineer Revenue Agent, dated March 12, 1942, in reference to the plaintiff's operations for the years 1939 and 1940, was furnished to the plaintiff. It contains the following recommendation:

> That the entire costs at December 31, 1940, in the Development and Jig Expense Account, including the losses incurred, not charged off in prior years, on the Airacuda and Airabonita models, be amortized at a rate represented by the ratio of planes produced during the year compared with the total of planes produced and on order at the end of the year.

This recommendation was in harmony with the plaintiff's original plan of amortization.

60 Under the aforesaid plan the amount of amortization applicable to each airplane produced and delivered would decrease from year to year in proportion to the total increase in the number of planes under contract at the end of each year. At the end of the year 1940, the plaintiff had contracted to deliver approximately 1600 airplanes under its fixed-price contracts.

14. During 1941, the plaintiff received an additional fixed-price contract W 535 ac–32 for 180 planes and equivalent in parts. This contract appears in the table of fixed-price contracts, Finding 9. In the latter part of the same year, the plaintiff entered into two cost-plus-fixed-fee contracts for 2,392 airplanes of a similar type. The plaintiff's officials were not certain that its amortization costs

would be approved for reimbursement under its CPFF contracts, and avoided any question of allowable reimbursements by limiting its amortization of the deferred charges to the fixed-price contracts only. The plaintiff added only the additional planes covered by the fixed-price contract entered into in 1941, and the amounts charged to each plane thereafter remained constant.

15. The plaintiff's annual reports which were prepared and certified to by Price, Waterhouse & Company, certified public accountants, contain the following explanatory comments regarding the treatment of experimental, development and production tooling costs:

ANNUAL REPORT FOR 1938

The company, from its inception, has charged currently to costs of contracts in progress all experimental and development work as the contracts were completed. During the year 1938 substantial experimental and development work of basic future value to the company was accomplished in connection with a contract for the design and construction of an experimental airplane. The total expenditures, including the costs for basic development above referred to, charged to the costs of such contract, plus the estimated costs to complete, amounted to $128,052.77 over and above the contract price of the experimental plane. The sum of $128,052.77 was transferred to a deferred account at December 31, 1938.

61 ANNUAL REPORT FOR 1939

C—The deferred experimental and development expenses were in respect of two experimental airplanes.

The first of these (known as the Airacuda) was practically completed at December 31, 1937, and the estimated excess of its cost over the contract sales price was charged to profit and loss accounts for the year 1937. Subsequent to the delivery of the airplane in 1938 expenditures were made in connection with improvements in design and in further development of this project. Such additional expenditures, amounting to $200,320.23 have been deferred at December 31, 1939, as, in the opinion of the management, the development of this type of airplane has a probable value to the Company in connection with expected future sales. A contract for 13 Airacudas for service test involving three experimental variations of the original Airacuda, now in progress, is expected to be completed during 1940. Since the date of closing the annual accounts the Company has made substantial expenditures, not theretofore anticipated, in connection with the contract for thirteen

Airacudas. The amount of the total excess costs over the contract price has not been determined at this time.

The second of the experimental airplanes is being constructed for the Navy and the amount of $217,682.92 deferred in respect to this airplane is the excess of the estimated total cost when completed over the contract sales price. In the opinion of the management, such excess costs constitute development and experimental expenditures of value in connection with expected orders for this or similar types of aircraft.

The amount of $128,052.77 deferred at December 31, 1938, in respect of another experimental airplane has now been transferred to costs of airplanes of similar type for which contracts were received in 1939; accordingly the amount deferred at December 31, 1938, is included in the inventory of work in progress at December 31, 1939.

It is the Company's intention to charge the deferred experimental and development expenses to costs of future production (exclusive of the service test order above referred to) or, if and when the projects are abandoned, to charge them off to profit and loss accounts.

ANNUAL REPORT FOR 1940

During the past five years, the Company has developed three types of Airplanes known as Airacobra, Airacuda, and Airabonita, all three incorporating certain similar basic new de-
62 velopments. In the opinion of the management the excess costs on experimental and service test contracts constitute experimental and development charges and, together with costs of tooling for production, have been deferred. Such costs amounted, in the aggregate, to $3,422,870.23 at December 31, 1940 and consisted of charges on the Airacobra of $2,123,195.87, on the Airacuda of $889,499.48 and on the Airabonita of $410,174.88. The Company is at present concentrating on the manufacture of Airacobras, and it is the Company's intention to absorb the aggregate of the foregoing charges on the basis of the quantities of this model under contract. Amortization amounting to $70,773.45 has been charged against cost of goods sold in 1940.

ANNUAL REPORT FOR 1941

Experimental, development and production tooling expenditures amounting to $3,352,096.78 were deferred at December 31, 1940, to be absorbed on the basis of certain quantities of aircraft under contract. Of this amount an amortization of

$1,998,184.02 applicable to aircraft delivered during 1941 was charged to cost of goods sold for that year.

During 1942, the plaintiff amortized the remaining experimental, development and production tooling costs in its deferred account against deliveries of airplanes under its fixed-price contracts.

16. Thus at the end of 1942, the plaintiff had amortized its entire deferred costs for experimental, development and production tooling against deliveries under its fixed-price contracts, as follows:

Contract number	1940	1941	1942	Totals
United States				
W 535 ac-12635	$27,880.45	$ 1,923.18	.....	$ 29,803.63
W 535 ac-13383	42,893.00	128,853.06	.....	171,746.06
W 535 ac-15675	.....	934,665.48	$ 382,712.82	1,317,378.30
W 535 ac-32	.....	.....	346,172.40	346,172.40
Totals	70,773.45	1,065,441.72	728,885.22	1,865,100.39
British				
A-218	.....	369,250.56	15,385.44	384,636.00
A-1326	.....	405,790.98	75,004.02	480,795.00
A-1476	.....	157,700.76	534,638.08	692,338.84
Totals	.....	932,742.30	625,027.54	1,557,769.84
Totals	70,773.45	1,998,184.02	1,353,912.76	3,422,870.23

63 COST-PLUS-FIXED-FEE CONTRACTS

17. In the meantime, commencing August 14, 1941, the plaintiff had entered into a series of cost-plus-fixed-fee, or CPFF, contracts with the defendant through the United States Army Air Corps for the production of P–39 or Airacobra airplanes.

Under the CPFF contracts the defendant agreed to reimburse the plaintiff for the cost of manufacturing and in addition to pay the plaintiff a fixed fee as provided in each of such contracts. The particular contracts, with dates of execution, are described in the following table:

Item	Date of contract	Contract numbers	Airplanes and equivalent in spare parts	Type	Estimated Costs	Fixed fee specified
(I).....	8/14/41	W 535 ac-20910	1,980	P-39D....	$70,960,740	$4,257,644.40
(J).....	9/10/41	DA W 535 ac-156 ..	412	P-39D-1 .	14,985,926	899,155.56
(K).....	6/29/42	W 535 ac-29318	2,700	P-39E ...	88,670,000	3,546,800.00
	4/13/43	Increase	2,470	P-63A-1 .	64,814,800	2,592,592.00
(L).....	9/28/43	W 535 ac-40071	2,600	P-39Q ...	68,387,200	2,735,488.00
Totals.....	.....	.....	10,162	.....	307,818,666	14,031,679.96

By supplemental agreement dated September 29, 1942, contract W 535 ac–29318 was changed to provide for deliveries of Model P–63A–1 in lieu of the P–39 type specified under the original contract. Contract W 535 ac–40041, dated January 5, 1944, for 2,470 planes and equivalent in spare parts, type P–63A–1, was combined on April 13, 1945, and made a part of contract W 535 ac–29318 and is represented by the increase as noted in the above table.

The production of P39 models was discontinued in April 1944 on all of the above-described contracts and changed over to P–63 models on which production was thereafter continued.

Deliveries were completed under contract DA W 535 ac–156, W 535 ac–40071 was terminated November 3, 1944, and contracts W 535 ac-20910 and W 535 ac-29318 were terminated for the convenience of the Government August 14, 1945. Termination settlement agreements were consummated pursuant to the Contract Settlement Act of 1944.

64 The foregoing contracts are filed as Exhibits I, J, K, and L, respectively, with Plaintiff's Exhibit 1 (the stipulation of facts) and are made a part hereof by reference.

18. Each of the CPFF contracts contains the following provisions:

ARTICLE 3. CONSIDERATION

* * * * *

(b) For the purpose of determining the amount payable under this Contract, allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a Contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T.D. 5000 and approved by the Secretary of War August 2, 1940. It being understood and agreed without limiting the generality of the foregoing, that

(1) All costs which have been incurred by the Contractor in anticipation of this Contract and prior to the signing thereof, and which if incurred after the signing of this Contract, would have been considered as allowable items of cost within the meaning of said Regulations, shall be considered as allowable items of cost incurred hereunder.

Article 3 (b) (2) of contracts W 535 ac–20910 and DA W 535 ac-156, and Article 3 (d) of contracts W 535 ac-29318 and W 535 ac-40071 provide:

(2) Any cost incurred by the Contractor under the terms of this Contract which would constitute an allowable item of

cost under the provisions of paragraph (b) of this article shall be included in determining the amount payable under this Contract, notwithstanding any provisions contained in the specifications or other documents incorporated in this Contract by reference, designating services to be performed or materials to be furnished by the Contractor at its expense or without cost to the Government.

Section 26.9 of Chapter 1 of Title 26, Code of Federal Regulations, as contained in T. D. 5000, is a promulgation of regulations governing the computation of Excess Profits Taxes, and provides, in part, as follows:

(d) *Other manufacturing cost.*—Other manufacturing cost as used in paragraph (b) of this section includes items of
65 manufacturing costs which are not properly or satisfactorily chargeable to factory costs (see paragraph (c) of this section) but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, payments of royalties and amortization of the cost of designs purchased and patent rights over their useful life; and "deferred" or "unliquidated" experimental and development charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. In the case of general experimental and development expenses which may be charged off currently, a reasonable portion thereof may be allocated to the cost of performing the contract or subcontract. If a special experimental or development project is carried on in pursuance of a contract, or in anticipation of a contract which is later entered into, and the expense is not treated as a part of general experimental and development expenses or is not otherwise allowed as a cost of performing the contract, there clearly appearing no reasonable prospect of an additional contract for the type of article involved, the entire cost of such project may be allowed as a part of the cost of performing the contract.

Said Section 26.9 of T. D. 5000 further provides in subparagraph (g) (4) thereof as follows:

• • • Among the items which shall not be included as a part of the cost of performing a contract or subcontract or consid-

ered in determining such cost, are the following: * * * losses on the other contracts; * * *

19. CPFF contracts W 535 ac-20910, DA W 535 ac-156, and W 535 ac–29318, provide in Articles 16 and 17 (a) thereof, as follows:

ARTICLE 16. DISPUTES

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the Contracting Officer, subject to written appeal by the Contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon
66 the parties hereto. In the meantime the Contractor shall diligently proceed with performance.

ARTICLE 17. DEFINITIONS

(a) The term "head of the department" as used herein shall mean the head or any assistant head of the executive department or independent establishment involved, and the term "his duly authorized representative" shall mean any person authorized to act for him other than the Contracting Officer.

CPFF contract W 535 ac–40071 provides in Article 16 thereof, as follows:

ARTICLE 16. DISPUTES

Except as otherwise specficially provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. * * * Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

REALLOCATION OF DEFERRED COSTS TO ALL PRODUCTION CONTRACTS

20. In 1942, at which time the plaintiff was engaged in production on CPFF contracts described in Finding 17, the Internal Revenue Bureau of the Treasury Department required that, for income tax purposes, the experimental, development and production
67 tooling expenses should be allocated to airplanes produced under CPFF contracts as well as the fixed-price contracts. The Plaintiff declined to accept this ruling and continued to amortize the remaining deferred charges for experimental, development and production tooling costs against the deliveries of airplanes under its fixed-price contracts during the remaining months of 1942, as set forth in Finding 16. The Bureau of Internal Revenue, however, adjusted the plaintiff's income for 1941 and 1942 for amortization by allocating such costs to deliveries under fixed-price contracts and deliveries made and to be made under CPFF contracts. Additional taxes assessed and paid for 1941 and 1942 totaled approximately $1,337,474.89.

21. On September 19, 1942, Charles L. Beard, then Secretary and Treasurer of the plaintiff corporation, in a memorandum directed to John Berry, Jr., Comptroller of the plaintiff corporation, made *inter alia* the following statement of policy in connection with such deferred experimental, development and production tooling expenses as it related to the above-mentioned suggestion then being made by the Bureau of Internal Revenue:

> This item should be allowed as an amortization expense against the fixed price contracts only in view of the fact that any amortization to be allowable under a cost-plus-fixed-fee contract would have to be included in the original negotiations of such contract. No provision is made for that on any of our cost plus contracts in view of the position taken by the Government that prior to our entry into cost plus contracts we have received sufficient fixed price contracts to permit the amortization of deferred experimental expenses.

On April 2, 1943, John Berry, Jr., prepared and submitted to the Resident Auditor, Army Air Forces, a "Statement of Accounting Policies, Pertinent to Operations Under Cost-Plus-A-Fixed-Fee Supply Contracts," in which he made the following statement in connection with deferred charges for experimental, development and production tooling expenses:

> 3. Deferred charges.—
>
> • • • • •
>
> (c) Experimental, development and production tooling ex-
> 68 penses are written off against the deliveries of the items to

which expenditures apply. No experimental expense is charged to overhead applicable to CPFF contracts. • • •

22. On September 7, 1943, the plaintiff wrote to the Price Adjustment Board, War Department, New York City, an outline of its proposed future amortization of said deferred charges. Major Knox B. Phagan was at that time Army Air Corps Price Adjustment Officer. Said letter is as follows:

Pursuant to our telephone conversation this afternoon, we should be glad if you would indicate your approval of the method to be followed in amortizing development and experimental expenses and production tooling costs of P–39 airplanes.

Our records as of December 31, 1942, and the schedules originally submitted to you showed that we had amortized the full amount of these costs against fixed price contracts. You objected to such treatment on the ground that the costs should be amortized over cost plus a fixed fee as well as fixed price contracts. The Bureau of Internal Revenue in examining our Federal income and excess profits tax return for the calendar year 1941 had made the same objection and required us to amortize the costs over all airplane contracts then held by us. In view of the position taken by the Bureau of Internal Revenue and yourselves we have agreed to amortize the experimental and development expenditurs over all contracts for P-39 and P-63 airplanes and the P-39 production tooling expenditures over all contracts for P–39 airplanes, provided that the amounts disallowed by you against fixed price contracts become items of reimbursable costs under our cost plus a fixed fee contracts and are allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office.

Under date of August 14, 1943 we provided you with two schedules which set forth in detail the amounts and contracts involved in the write-off from January 1, 1940, to June 30, 1943, on an actual write-off basis and through the balance of 1943 and 1944 on an estimated basis.

The method agreed upon involved a determination of each of the two amounts involved, which amounts are as shown by our books (and less adjustments aggregating $2,892.19 are as shown by a report of an Agent of the Bureau of Internal Revenue as of December 31, 1940) less adjustments made by the
69 Contract Audit Section of the Army Air Forces as a result of their examination of the costs. The amounts are as follows:

	Development and experimental	P-39 production tooling	Together
Costs to December 31, 1940 (there were no additions subsequently)	$1,528,760.66	$1,894,109.57	$3,422,870.23
Less—Costs disallowed by Contract Audit Section, Army Air Forces	29,021.43	19,383.80	48,405.23
Amount to be amortized as agreed upon with Price Adjustment Board and Contract Audit Section, Army Air Forces	1,499,739.23	1,874,725.77	3,374,465.00

The last amounts shown above are to be amortized over all fixed price and cost plus a fixed fee supply contracts for P-39 and P–63 airplanes as follows:

The sum of the number of airplanes and equivalents on order and undelivered at the beginning of the year and the number of airplanes and equivalents ordered during the calendar year is to be divided into the unamortized cost as of the beginning of the year, the resulting quotient represents the amortization per airplane. The amortization per airplane multiplied by the number of airplanes and equivalents accepted by the Army Air Forces during the period for each contract results in the amortization per contract.

We believe the foregoing sets forth the understanding between us as to the amortization of the expenditures for experimental and development and P–39 production tooling and if it is in accordance with your understanding we should like you to so indicate by signing one copy of this letter and returning it to us.

Yours very truly,

BELL AIRCRAFT CORPORATION,
(Signed) JOHN BERRY, JR.,
Comptroller.

The explanation and method of amortization set forth in this letter is in accordance with our understanding and has our approval.

(Signed) KNOX B. PHAGAN,
Maj. A. C., Price Adj. Officer.

Date: Sept. 9, '43.

The plan of amortization outlined in the above letter is in accordance with the decision of the Internal Revenue Bureau. It was the plaintiff's original plan of amortizing these costs
70 against production under fixed-price contracts before it had

received any of its CPFF contracts. Major Phagan was then Chief of the Price Adjustment Section, Eastern District, Air Forces.

23. On September 9, 1943, the plaintiff's comptroller issued instructions for the restoration to the deferred account the proportion of experimental, development and production tooling which became applicable to airplanes delivered and to be delivered under the CPFF contracts, in accordance with the approved plan of reamortization. There was restored the sum of $2,286,819.95, consisting of:

Experimental and development costs	$1,035,918.73
Production tooling for P-39 planes	1,250,901.22

The unrestored difference of $1,087,645.05 previously amortized represented that portion of experimental, development and production tooling which was applicable to deliveries under the fixed-price contracts in accordance with the approved plan of reamortization.

Reimbursement vouchers were prepared by the plaintiff and submitted in the sum of $451,179.96 for reallocation of amortization of experimental, development, and production tooling on deliveries under CPFF contracts during 1942 and $848,676.06 for deliveries under CPFF contracts during January to August, inclusive, of 1943, as follows:

Contract numbers	Experimental and development expenses	Production tooling costs	Total
W 535 ac-20910	$370,552.30	$819,571.64	$1,190,123.94
DA W 535 ac-156	37,318.96	72,413.12	109,732.08
Total	407,871.26	891,984.76	1,299,856.02

The defendant's Contracting Officer approved the above vouchers for reimbursement under the CPFF contracts, and the plaintiff was paid the said sums by the defendant's Finance Officer.

24. Commencing in October 1943, the plaintiff submitted additional reimbursement vouchers for experimental, development, and tooling costs, representing the proportionate
71 amounts applicable to deliveries subsequent to August 1943 under CPFF contracts, as follows:

Contract numbers	Experimental and development expenses	Production tooling costs	Total
W 535 ac-20910	$194,947.81	$ 79,991.20	$274,939.01
DA W 535 ac-156	13,888.85	4,371.50	18,260.35
W 535 ac-29318	223,288.09	69,895.04	293,183.13
W 535 ac-40071	195,922.72	204,658.72	400,581.44
Total	$628,047.47	$358,916.46	$986,963.93

The above sums represent vouchers for all of the remaining experimental, development, and production tooling costs for which the plaintiff claimed reimbursement. No part of these sums has been paid.

25. As these vouchers began to arrive for audit in October 1943 the defendant's Resident Auditor, Roland Campbell, had been replaced by Frank Ferris. About the same time, Bancroft Mitchell, the Contracting Officer for the plaintiff's CPFF contracts, was replaced by Maj. Harold B. Davies, who acted both as Administrative Contracting Officer and Termination Contracting Officer.

The Assistant to the Resident Auditor, James D. DiLapo, recommended against approval of these vouchers for reimbursement on the ground that the plaintiff had consistently charged its experimental, development and production tooling costs against deliveries under its fixed-price contracts, and for the further reason that DiLapo considered such costs as losses on other fixed-price experimental contracts which would not be reimbursable costs under CPFF contracts. Approval of these vouchers was withheld by Ferris.

In February 1944, the defendant's Resident Auditor Ferris was replaced by one Harry Liebman, who likewise withheld approval of these vouchers on the ground that the CPFF contracts contained no provision for payment of experimental, development and production tooling expenses, except by reference to T. D. 5000, and for the further reason that the plaintiff had previously amortized such costs against fixed-price contracts.

Major Davies declined to approved these vouchers, since these deferred costs had been previously amortized against
72 deliveries under fixed-price contracts, and he thought the plaintiff had changed its method for the reamortization of such costs over all contracts as a result of the decision of the Bureau of Internal Revenue, but without the approval of the Contracting Officer. By his decision of March 1, 1945, the Contracting Officer denied the plaintiff's claim for reimbursement of these vouchers.

26. In April and May 1944, the Chief Cost Auditor for the General Accounting Office, Buffalo area, submitted to the Resident Auditor a series of "informal inquiries" in respect to the reimbursements of experimental, development and production tooling costs by Col. J. Harris, Finance Officer, in August and September 1943, summarized in Finding 23, as follows:

		Reimbursement exceptions	
Informal inquiry	Dated	Contract	Total payments
777	4/25/44	W 535 ac-20910	$1,064,888.18
778	4/25/44	DA W 535 ac-156	109,732.08
789	5/13/44	W 535 ac-20910	125,235.76
Total (Finding 23)			$1,299,856.02

Each of the foregoing inquiries made exception to such payments as follows:

> Since the entire amount of the Deferred Experimental and Development Expenses and the Production Tool Expenses were amortized or written off against prior commercial and Government fixed price contracts by the contractor, the status of the account at the time of the negotiations with respect to the estimated costs under his contract was such as to preclude consideration thereof as an existing "Deferred" or "unliquidated" charge to the contract and the fact that for tax purposes the account was reopened and amortized in part against this contract would appear to afford no proper basis for considering the amount so amortized as a reimbursable item of cost under this contract.

27. By letters dated June 29, 1944, the Resident Auditor, Harry Leibman, advised the Chief Cost Auditor for the General Accounting Office at Buffalo that deductions were made on vouch-
73 ers listed in the said letters to recover payments for experimental, development and production tooling costs, in accordance with informal inquiries 777, 778 and 789. Copies of these letters were furnished the plaintiff.

The Contracting Officer held up the vouchers on which the Resident Auditor made deductions, and took no action upon them until September 1944.

In the interim the Comptroller General of the United States issued formal notices of exception and suspensions of the accounts of Colonel J. Harris, Finance Officer at Buffalo, dated August 18, 1944. These notices covered the sums of $1,064,888.18 and $109,732.08, on which exceptions were noted by informal inquiries Nos. 777 and 778 and for the same reason. They were received by the Finance Officer August 21, 1944. Recoupment of these sums was made immediately by the Finance Officer on vouchers for monies otherwise due the plaintiff, and the Comptroller General was advised thereof by reply endorsements August 25, 1944.

On September 6 and 8, 1944, the Contracting Officer transmitted to the Finance Officer for settlement, groups of the plaintiff's vouchers, which included the vouchers on which deductions were made by

the Resident Auditor, as above. The Contracting Officer reinstated vouchers for $1,064,888.18 and $109,732.08 for which sums had been recovered by the Finance Officer, but other deductions for $125,235.76 were approved by him in compliance with informal inquiry and exception No. 789, and in harmony with the formal notices of exception and suspension previously received by the Finance Officer.

On September 12, 1944, the Finance Officer received a formal notice of suspension from the Comptroller General dated September 11th for the sum of $125,235.76, in accordance with informal inquiry No. 789. A reply endorsement was issued the following day by the Finance Officer for removal of the suspension since this sum had been deducted from vouchers for amounts otherwise due the plaintiff. Thus the payments totaling $1,299,856.02 for experimental, development and production tooling costs reimbursed to the plaintiff on CPFF contracts were fully recovered by the defendant.

74 28. Experimental, development, and production tooling costs which were amortized and vouchered for reimbursement by the plaintiff under CPFF contracts, Findings 23 and 24, are combined as follows:

Contract number	Experimental and development expense	Production tooling costs	Total
W 535 ac–20910	$ 565,500.11	$ 899,562.84	$1,465,062.95
DA W 535 ac–156	51,207.81	76,784.62	127,992.43
W 535 ac–29318	223,288.09	69,895.04	293,183.13
W 535 ac–40071	195,922.72	204,658.72	400,581.44
Total	$1,035,918.73	$1,250,901.22	$2,286,819.95

29. The Contracting Officer declined to approve the additional vouchers for $986,963.93 (Findings 24 and 25), and on March 1, 1945, issued his decision denying any reimbursement. This decision states in part:

> It appears that the said sum of $2,286,819.95 which Bell has charged on its books against CPFF contracts does not, in fact, represent costs of performing such CPFF contracts and that reimbursement for such costs under the said CPFF contracts would result in Bell's receiving double payment from the Government therefor.

The sum of $2,286,819.95 represents the $1,299,856.02 which had been approved by the predecessor Contracting Officer, paid, and recouped by the Finance Officer under suspension by the Comptroller General, as well as the unpaid vouchers totaling $986,963.93, summarized in Finding 24, for which no payment had been made.

30. On March 27, 1945, the plaintiff made timely appeal from the findings and decision of the Contracting Officer, in denying payment on vouchers totaling $986,963.93. The sum of $1,299,856.02, which had been previously reimbursed and was noted for exception and suspension of the accounts of the Finance Officer by the Comptroller General, was not appealed by the plaintiff nor considered by the War Department Board of Contract Appeals, representing the Secretary of War.

On April 29, 1946, the War Department Board of Contract Appeals rendered its decision on the plaintiff's appeal in
75 which it denied the reimbursement of the said sum of $986,963.93. This decision states in part:

> The experimental and development costs are clearly within the category of indirect costs as defined by T. D. 5000 and are specifically covered by Section 26.9 (d) of T. D. 5000—set out above. There is no specific reference in T. D. 5000 to the amortization of production tooling costs and appellant has not pointed out a specific provision of T. D. 5000 which it considers as providing for the allowance of such an item of cost. In the pamphlet issued by the War and Navy Departments entitled "Explanation of Principles for Determination of Costs Under Government Contracts" (Par. 18), it is indicated that items such as royalties and the amortization of the initial cost of dies, patterns, and special tools can logically be classified as direct shop costs and be charged to contracts on an equitable basis of apportionment. Section 26.9 (c) (5) (D of T. D. 5000 set out above also provides that charges for depreciation of property used in the manufacturing process may be treated as an item of cost. It is clear from the record and evidence that the production tooling was used in the performance of CPFF contracts calling for the production of the P–39 type of airplane. It would seem, therefore, that items of this type are within the intent and meaning of T. D. 5000.
>
> • • • • •
>
> Although it is true that costs of this type may properly be allowed as reimbursable items under T. D. 5000, it does not follow that such costs must be reimbursed under T. D. 5000 in all cases and under all circumstances. In order to determine whether such items of costs should be reimbursed it is necessary to examine all of the circumstances and facts involved. The subject costs—both engineering and development, and production tooling costs—were incurred a considerable time before any of the CPFF contracts were entered into. The production tooling costs were incurred for the express and admitted purpose of performing certain fixed-price contracts then on hand

or in process of negotiation. They were not incurred in anticipation of the CPFF contracts and would have necessarily been incurred regardless of whether any further contracts for the P–39 type of airplane were received or not. The engineering and development costs were incurred during the period 1938 to 1940 and the costs were capitalized because it was
76 felt that the development in connection with which they were incurred had a probable value in connection with expected future sales. In 1940 appellant entered upon a course of conduct by which these costs were charged against certain fixed-price contracts. The procedure of charging these costs against fixed-price contracts was continued during 1941 and 1942 in accordance with the mentioned plan to the effect that at the end of 1942 all of the costs in question had been absorbed. During this period some of the subject CPFF contracts were entered into and all of them were negotiated prior to August of 1943 at which time appellant changed its plan of amortization to the one now contended for. It is clear from the record that no portion of these costs was included in the estimates under the CPFF contracts and no specific consideration was given to the question of reimbursement in the negotiation of the subject contracts. It also may be reasonably concluded that appellant had no intention, at the time the contracts were entered into, of seeking reimbursement for such costs since its accounting method did not contemplate reimbursement.

• • • • •

For the reasons herein set out the appeal insofar as it relates to contracts numbered W 535–ac–20910, W 535–ac–29318, W 535–ac–40071, and W 535–ac–40041 is denied.

In respect to contract DA W 535 ac–156, the President of the Board, the duly authorized representative of the Secretary of War, decided in accordance with the entire Board on other contracts, and denied the plaintiff's appeal insofar as it related to this contract.

The plaintiff's application for a rehearing was denied by the Board May 31, 1946.

This decision is in evidence as Exhibit P to the stipulation (Plaintiff's Exhibit 1) and is incorporated herein by reference.

31. As heretofore related (Finding 17) all of the CPFF contracts were terminated for the convenience of the Government upon termination of hostilities. Termination settlement agreements were entered into pursuant to the Contract Settlement Act of 1944, in which the plaintiff made reservations in respect to its claims for reimbursements under the CPFF contracts, as follows:

The Supplemental Settlement Agreement dated December 21, 1945, covering the termination of contract W 535 ac-
77 20910, contains the following reservation in Article 4 (c) (2) (b):

> Claim for experimental and development and research costs in the amount of $1,465,062.95 which is now the subject of an appeal pending before the War Department Board of Contract Appeals.

The Supplemental Settlement Agreement dated May 15, 1946, covering the termination of contract W 535 ac–29318, contains the following reservation in Article 4 (c) (2) (b):

> $293,183.13 of experimental and development expenses now the subject of an appeal pending before the War Department Board of Contract Appeals.

The Supplemental Settlement Agreement dated February 22, 1946, covering the termination of contract W 535 ac–40071, contains the following reservation in Article 4 (c) (2):

> Claim by the Contractor against the Government, as to which his right of reimbursement is disputed, which is excluded without prejudice to the rights of either party, to wit, claim for experimental and development and research costs in the amount of $400,581.44, which is now the subject of an appeal pending before the War Department Board of Contract Appeals.

These termination settlement agreements are attached to the respective contracts to which they pertain, as Exhibits I, K, and L to the stipulation filed and are incorporated herein by reference.

At the time the settlement agreement was consummated for contract W 535 ac–20910, there was pending before the War Department Board of Contract Appeals the plaintiff's claim for reimbursement of costs for $274,939.01. The difference of $1,190,123.94 had been reimbursed to the plaintiff, but was recouped by the Finance Officer upon notice of exceptions and suspension by the Comptroller General.

32. On March 27, 1945, the plaintiff executed a renegotiation agreement pursuant to Section 403 of the Sixth Supplemental National Defense Appropriation Act, 1942, as amended, in respect to excessive profits for its fiscal year ending December 31, 1942. This agreement was signed by Colonel Maurice Hirsch, G. S. C., for all services of the United States concerned, and was approved for the Under Secretary of War May 22, 1945. The said agree-

78 ment is in evidence as stipulation Exhibit N, attached to the Plaintiff's Exhibit 1, and is incorporated herein by reference. The said agreement covered profits for 1942 on both fixed-price contracts and CPFF contracts with the United States. It provided for refund by the plaintiff of $7,714,000 of excessive profits for the year 1942, after first applying the tax credit applicable to such profits. This agreement provides in part: (See also Finding 16 herein.)

EXHIBIT "C"

• • • • •

PRINCIPLES UNDERLYING SEGREGATION OF SALES AND PROFITS

• • • • •

Allcation of Cost of Sales and Expenses

1. *Cost of sales:*

• • • • •

(g) Deferred Experimental Development, and Production Tooling Expenses in the amount of 1,353,913 were amortized over all planes delivered under Fixed Price Contracts during the year. For the purpose of computing the additional refund under Paragraph VIII of the Agreement, the adjusted amortization chargeable to 1942 of 638,683 was allocated on the basis of the total number of planes delivered under all contracts, both Fixed Price and CPFF.

• • • • •

VIII. In arriving at the refund herein the items of Deferred Experimental Develpoment, and Production Tooling Expenses in the amount of $728,885.22 have been charged as Costs against Renegotiable Fixed Price Contracts for said fiscal year. The Contractor, in order to conform its method of handling these items to the method adopted by the Bureau of Internal Revenue, has adjusted its figures for said fiscal year by amortizing these items over the total number of planes of the Airacobra type produced, or to be produced, on both Fixed Price and CPFF Contracts (Production Tooling limited to P–39 Models). Such method of amortization and the corresponding reallocation of costs to CPFF Contracts, as well as Fixed Price Contracts, has been tentatively approved by the Army Air Forces, and if the amount allocated to the CPFF Contracts is finally approved by both the Army Air Forces and the General Accounting Office of the Comptroller General of the United States, and reimbursement therefor, is made,
79 the Contractor agrees to pay to the United States as an ad-

ditional refund the sum of $667,000, on account of which the Contractor shall receive credit for Federal Income and Excess Profits Taxes thereon as determined by the Bureau of Internal Revenue as provided in Paragraph VII hereof.

33. The amortization allowance of experimental, development and production tooling to fixed-price contracts only under the foregoing settlement agreement was contrary to the allocations by the Bureau of Internal Revenue, which amortized these costs upon production for all contracts.

As a result of a plan applied by the Bureau of Internal Revenue, additional assessments were made against the plaintiff's income for 1941 and 1942 in the approximate sum of $1,337,474.89. By deducting amortization which it allocated to production under CPFF contracts, assessments were reduced for the years 1943, 1944 and 1945 by the approximate sum of $1,305,418.72. The net increase in tax assessments was approximately $32,056.17.

The amortization by the Bureau of Internal Revenue was applied as a deduction against the plaintiff's net income from the fixed fees under CPFF contracts, whereas, the plaintiff claims that no reduction should have been made to its fixed fees on account of amortization, but that the full sum of $2,286,819.95 should have been reimbursed as a portion of its costs of performing these contracts.

VALUE OF EXPERIMENTAL AND DEVELOPMENT WORK TO COST-PLUS-FIXED-FEE CONTRACTS

34. Experimental and development costs capitalized and deferred by the plaintiff for allocation to future production were not segregated as between specific experimental contracts to which they might apply. It was impossible to make any reasonably correct segregation of such costs, since the improvements in design and fabrication developed in the earlier operations were carried forward and applied on later experimental and development work, and finally into production contracts. These costs represent deferred values of designing and experience in fabrication rather than costs of any particular airplane contract.

The plaintiff took over the plant on Elmwood Avenue, Buffalo, New York, in the fall of 1935, which had been
80 vacated by Consolidated Aircraft Company upon its transfer to California, and an abundance of experienced personnel who elected to remain in Buffalo.

The plaintiff's first work involved the installation of an Allison model engine in the nose of a Consolidated airplane. It was the first installation of this kind for the Allison model, which was a heavy 1,000 h. p. engine, whereas other models previously used were

normally about 600 h. p. models. It required investigation of the strength of the wings, tail, fuselage and landing gear. The plaintiff's next job was subcontract work for manufacturing all-metal, aluminum, riveted wings for Consolidated flying boats.

The first experimental plane was the XFM–1 Airacuda contracted for May 12, 1936. It was substantially completed by the end of 1937. All costs of experimental and development work on the above projects were charged against these contracts currently or to the plaintiff's profit and loss account, up to and including December 31, 1937. The plaintiff continued further development work on the XFM–1 model in 1938, and later on a contract for service test models of the same type.

35. Some of the basic principles of design and fabrication, which the plaintiff developed on experimental contract work and incorporated into the P-39 production models, include the following:

(a) The installation and successful operation of a liquid-cooled Allison engine, involving installation problems and other features of design necessary to operations.

(b) The extension of the drive shaft, so that the propellers could operate more distant from the engine.

This feature was designed on the XFM-1, where the engine was housed in the wing structure, and the pusher-type propellers operated from the rear of the wings. The extension drive shaft was adopted in the P-39, by locating the engine in the fuselage to the rear of the pilot, with the extended drive shaft projected beneath the pilot and operating the propeller in the nose of the aircraft, thereby providing vision for the pilot and permitting the projecting nose of the plane to better accommodate the front wheel of the tricycle landing gear.

81 (c) The design and successful installation of air intake ducts for cooling the engine and oil systems, known as "ducted radiator", whereby an intake opening was provided in the leading edge of the wing for admitting air at high velocity.

The air then expanded into larger internal ducts slowing down its velocity for cooling purposes. The overhead air scoop was subsequently incorporated in all P-39's and P-63 planes. The intake was provided on top of these planes, instead of the front edge of the wing, but serving the same purpose of obtaining a simple duct system of air intake to the carburetor of the engine.

(d) The development and installation of a successful anti-shimmy dampening device for the nose wheel of the tricycle landing gear.

The nose wheel of this type of gear was provided with a swivel stirrup to steer the plane on the ground. The nose-wheel shimmy or oscillation was inherent in this type of gear, as the plane would take the runway at high speed or over rough roads. The first successful development of the shimmy dampening device was in connection with the XP-39, although the basic characteristics in this device were developed by the plaintiff in connection with the development and installation of a shock-absorbing gun mount for the XFM-1 plane.

(e) The successful installation of a 37mm. repeating cannon in the XFM-1.

In the flexible gun mountings for the Airacudas the plaintiff devised means of holding and supporting the gun so that it could be properly aimed and provided for the recoil in this type mounting. In the P-39's it was installed in a fixed mounting, but other features of feeding and ejecting the heavy empty cartridges were retained. Provision was made for retaining in the plane the empty shells that were ejected from the cannon, to avoid fouling or damage to the plane when they were ejected. In lieu of clips, which required manual changing, the plaintiff devised an automatic feed belt to carry the shells into firing position.

(f) Flush riveting, which was developed in the earliest experimental planes, was carried into all later production.

A high-strength aluminum alloy was specified for the
82 XFM-1 fighter plane built by the plaintiff under its first experimental contract. In order to take advantage of the higher structural tensility of this material the plaintiff, by a process of heat treating, sunk the rivets approximately flush with the surface of the metal, which resulted in a smoother external surface in this type of fabrication.

(g) In the construction of the XFL-1 Airabonita, the plaintiff designed and provided very heavy-duty landing gear to accommodate, without undue hazard, the catapult, deck landing and arresting equipment. This tougher type of landing gear was subsequently provided for P-39 models using the tricycle landing gear.

In connection with the XFL-1 for the Navy, the plaintiff also developed a nose-over beam, which extended in the fuselage above and behind the pilot for his protection in case the plane turned over. This feature was also incorporated in the production models of P-39 Airacobras.

(h) Engineering standards which were prepared for experimental work, consisting of short-cut repeat operations, tables and curves of technical information.

Once computed, these standards could be applied thereafter without recalculations.

(i) The earlier Allison engines furnished the plaintiff attained their greatest power at sea level.

In order to give them more power at high altitudes, the plaintiff installed General Electric turbo superchargers which were operated from the engines. Later Allison engines incorporated features to provide power at high altitudes, which duplicated the external unit and voided its further use.

(j) The plaintiff also developed and provided compartments in the wing structure of the experimental planes for carrying additional fuel, known as integral fuel tanks.

There were designed to be liquid tight and were enclosed by integral parts of the plane structure, such as the inside beams, bulkhead and outside sheeting. This feature was installed in P-39 models but it was not satisfactorily perfected because of difficulty with leakage, and was later superseded with bullet-proof storage tanks, by fitting the compartments with rubber and composition cells that would self seal any bullet penetration.

83 With the exception of the last two features above, the developments, engineering standards and fabricating processes acquired during the manufacture of experimental airplanes were incorporated and utilized on all production. The measure of value to production after 1940 is represented by the plaintiff's excess of costs on experimental airplanes over and above its recoveries under these contracts in the net amount of $1,499,739.23.

36. The plaintiff obtained a basic patent on its development of a hydraulic shimmy-dampening device in the steering mechanism of the nose wheel of the tricycle landing gear, and certain other patents for semi-automatic counter sinkers, twisted spar mills, routers and stake drills. It recovered substantial royalty payments for use of these devices by another manufacturer. As a result of proceedings before a Royalty Adjustment Board, the plaintiff was required to pay over to the Government some $691,666.24, under an indemnity agreement with the War and Navy Departments, representing all royalties collected by it.

There was included in the sums paid over one amount of $102,050.28, which the plaintiff had previously taken into its income and paid taxes thereon. The tax rate during the war years averaged approximately 70 percent of the plaintiff's total net income. No part of the royalties collected was retained by the plaintiff.

The Government also received credit of $360,000 on a contract for an improved model of the P-39, pursuant to an agreement with

the plaintiff dated April 11, 1940, which authorized the plaintiff to make certain deliveries to the British of the P-39 model airplanes in advance of deliveries under one of the production contracts for the Army Air Corps.

37. A fair measure of the value of experimental and development work applicable to all production contracts is to equalized profits realized by the plaintiff upon experimental and production fixed-price contracts.

After having amortized the total amount of experimental, development and production tooling expenses against its fixed-price production contracts, the plaintiff realized a net profit, before taxes and renegotiation of excess profits, of $18,280,732.50.

84 By adding back the experimental and development expense of $1,499,739.23, the profit would be $19,780,471.73, or 27.7 percent of the total value of $71,364,004.86 for these contracts.

The total value of experimental fixed-price contracts was $4,049,445. By applying the profit ratio of 27.7 percent, the plaintiff would have realized a profit of $1,121,696.27 on its experimental contracts. By adding to this sum the plaintiff's costs in excess of the prices realized on experimental contracts there is derived the sum of $2,621,435.50 for amortization over all contracts.

38. The plaintiff's net income on its fixed-price production contracts, after renegotiation and taxes, was approximately $4,637,607.63.

39. The sum of $1,499,739.23, which was capitalized and deferred by the plaintiff for allocation to future production, represented a fair and reasonable value of the general experimental and development work in benefits and savings on production contracts.

VALUE OF PRODUCTION TOOLING TO COST-PLUS-FIXED-FEE CONTRACTS

40. Production tooling for the P-39 model was provided during 1939 and 1940. At the end of 1940, the plaintiff capitalized and deferred for allocation to future operations, production tooling costs totaling $1,874,725.77.

This production tooling was used for the fabrication and assembly of airplanes under all of the fixed-price production contracts. Some of the tools other than assembly fixtures became worn out through use or became obsolete on account of current changes from time to time during production.

The major portion of tooling for the P-39 models was used throughout the production of this type of plane under the CPFF contracts. Where replacements or reworking of tools became nec-

essary, the costs were charged against current operations, so that when production under CPFF contracts was commenced the value of production tooling was substantially the same as when it was originally installed for use on fixed-price contracts.

In April 1944, the P-39 model was discontinued, and retooling became necessary for the production of P-63 models. All
85 tooling which could not be used in the production of the later model was scrapped and replaced upon approval of the defendant's plant clearance officer.

Lists of tools and equipment which could no longer be used on the new models were prepared by the plaintiff, and allocated to certain of the CPFF contracts then in process. The proceeds of the sale of these tools and fixtures were credited to the defendant on CPFF contracts.

The beneficial value of production tooling for P-39 model airplanes manufactured under CPFF contracts was at least equivalent to the beneficial use of such tooling to performance under the fixed-price production contracts.

41. In submitting bids for its fixed-price contracts the plaintiff also submitted data of estimated costs of performing these contracts, the details of which are appended to copies of these contracts. None of the estimates for performing the fixed-price contracts contain any provision for the amortization of experimental, development and production tooling costs.

Estimated costs in the cost-plus-fixed-fee contracts, as specified in Article 2 thereof, were based upon data on file in the office of the Chief of Air Corps, no details of which were attached to these contracts. There is no evidence that these data contained any estimate for the experimental, development and production tooling costs involved herein.

Article 3 (a) of the CPFF contracts provided for a fixed fee to the plaintiff of 6 percent of the estimated costs under the first two of these contracts and 4 percent of the estimated costs under the last two thereof. This Article contains the additional provision:

> • • • This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof; provided, however, that there shall be no adjustment in the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost or where the estimated cost varies from the actual cost.

The provisions for allowable costs are contained in the same article.

86 The plaintiff amortized its deferred costs for experimental, development and production tooling expense over all production contracts, as follows:

	Fixed-price contracts (Findings 12 and 23)	C P F F contracts (Finding 28)
Experimental and development expense....	$ 463,820.50	$1,035,918.73
Production tooling expense	623,824.55	1,250,901.22
	$1,087,645.05	$2,286,819.95

The amortization of $1,087,645.05 represents 1.52 percent of the total $71,364,004.86 value of fixed-price contracts, all of which were completed. The amortization of $2,286,819.95 on CPFF contract production represents .71 percent of the total estimated cost plus the fixed fees specified in these contracts. Deliveries called for under CPFF contracts were not completed and the contracts were terminated upon cessation of hostilities August 14, 1945.

The plaintiff's experimental, development and production tooling costs were properly deferred and included as an element of costs in performing its cost-plus-fixed-fee contracts. The amortization was applied in accordance with a reasonably consistent plan, ratably applied to the total number of P-39 model airplanes produced.

Respectfully submitted,

MARION T. BENNETT,
Commissioner.

87 ARGUMENT AND SUBMISSION OF CASE.

On January 11, 1951, the case was argued and submitted on merits by Mr. William M. Aiken for plaintiff; and by Mr. John B. Miller for defendant.

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89 *Special findings of fact, conclusion of law and opinion of the court by Howell, J. Dissenting opinion, in part, by Jones, Chief Judge. Dissenting opinion by Madden, J.*

BELL AIRCRAFT CORPORATION v. THE UNITED STATES

Mr. William M. Aiken for the plaintiff. *Messrs. Dudley, Stowe & Sawyer*, and *Messrs. Covington, Burling, Rublee, O'Brian & Shorb* were on the briefs.

Mr. John B. Miller, with whom was *Mr. Assistant Attorney General H. G. Morison,* for the defendant. *Mr. Thomas O. Fleming* was on the brief.

The Court, upon the evidence, the report of Commissioner Marion T. Bennett, and the briefs and argument of counsel, makes the following

SPECIAL FINDINGS OF FACT.

1. The plaintiff is a corporation organized and existing under the laws of the State of New York with its principal office and place of business in the Town of Wheatfield, Niagara County, New York.

2. The plaintiff was organized and commenced business in 1935, and thereafter, during all the times mentioned herein, the major part of the plaintiff's business has been the development and manufacture of military aircraft.

EXPERIMENTAL AND DEVELOPMENT COSTS DEFERRED

3. In 1936, 1937, and 1938, the plaintiff entered into certain experimental contracts with the defendant, through the United States Army Air Corps for the construction of certain
90 experimental and service test airplanes. Experimental airplanes were designated by the letter "X" preceding the model number, and the service test airplanes were designated by the letter "Y" preceding the model number. Other designations of type preceding the model number of particular airplanes hereinafter mentioned were "F" for "Fighter" and "P" for "Pursuit."

4. The following fixed-price experimental contracts were entered into between the plaintiff and the United States for fighter planes, in the performance of which the plaintiff incurred substantial expenditures over and above amounts received, which costs were set up on the plaintiff's books as deferred charges applicable to anticipated production:

Item	Date of contract	Contract numbers	Airplanes Units	Models	Designations	Contract price
(A)	5/12/36	W 535 ac-8773...	1	XFM-1	"Airacuda"	$ 390,300
(B)	9/27/37	W 535 ac-10341...	1	XP-39	"Airacobra"	245,880
(C)	4/20/38	W 535 ac-11122...	10	YFM-1	"Airacuda"	3,168,265
			3	YFM-1A		
(D)	11/8/38	63629	1	XFL-1	"Airabonita"	245,000
			16			$4,049,445

Contract No. 63629 was with the Navy, Bureau of Supplies and Accounts, and the others were with the Army Air Corps.

Articles 19, 21, 21, and 29, respectively, of the foregoing contracts provide for a nonexclusive, irrevocable right and license to the Government to use any and all discoveries, inventions, improvements and/or suggestions which are wholly or in part developed, perfected and/or reduced to practice with the aid and/or cooperation of the Government or of Government personnel, and/or by the contractor to meet explicit Governmental requirements or by the fulfillment of such contract.

Articles 26, 26 and 25, respectively, of the Army contracts provide:

> *Reproduction rights.*—It is understood and agreed that the contractor does not convey to the Government any reproduction rights in or to the articles and/or spare parts called for herein by virtue of the terms of this contract, except as hereinbefore set forth.

91 The plaintiff acquired a number of basic patents in connection with its development work, on which substantial royalties were realized.

5. All the airplanes delivered on these experimental contracts, as well as the production contracts received later, were powered by liquid-cooled Allison engines, furnished by the Government. The Government also furnished other materials and parts, consisting of the wheels, tires, tubes, propellors, guns, instruments and certain electrical and communications equipment.

The Airacuda was a twin-engine, five place. long-range fighter plane with pusher propellors operated by drive shafts to the engine. It was armed with two 37mm. repeating cannon, flexibly mounted in the nose of its engine nacelles, and two 50-calibre machine guns installed in the waist, with flexible mountings manually operated, with a wide sweep firing range upward, downward or rearward. These planes were originally designed with conventional landing gear, that is, with two wheels abreast, one under each wing and a tail wheel to carry the rear portion of the fuselage. The three YFM-1A service test model Airacudas incorporated the tricycle landing gear which had been developed in connection with the experimental Airacobra.

The Allison engines supplied for the experimental planes operated at maximum power at sea level. The plaintiff installed an external General Electric turbo supercharger, driven from the engine, which increased its power at high altitudes. Allison later delivered altitude-rated engines, which duplicated the external unit and voided its further use. Two of the service test Airacudas incorporated the altitude-rated engines. The Airacuda was approximately two and one-half times the weight of the Airacobra.

The Airacobra was a single-engine and propellor, single-seat, short-range interceptor fighter plane. The engine, mounted to the rear of the cockpit, operated the propellor at the nose of the plane by means of a drive shaft. A tricycle landing gear was developed in the experimental model which consisted of a retractable nose wheel and two retractable wing wheels. The Airacobra was armed with one 37mm. repeating cannon which fired through the shaft and hub of the propeller from a fixed mounting, and two
92 50-calibre machine guns which fired from fixed mountings between the propeller blades, so that the position of the plane governed the aim at a target, without any manual control.

The Airabonita was modeled after the Airacobra, but adapted to use on airplane carriers. The conventional landing gear was restored to this model and a tail hook was provided to engage the carrier deck arresting gear for landing purposes.

6. The first experimental Airacuda had been substantially completed by the end of 1937, and the excess of costs over the contract price for this unit was charged to profit and loss accounts for that year. Subsequent to the delivery of this airplane in 1938, the plaintiff incurred additional expenditures for the development and improvement in this design. The plaintiff's expenditures for the 13 test models of this design were also substantially in excess of the contract price received. These excess costs were capitalized as "deferred charges" in 1939 and 1940 for distribution as an element of cost against future production.

Much of the basic engineering and development designing in the Airacuda was carried forward and incorporated in the Airacobra which later entered quantity production for the Army Air Corps and the British Government.

The tooling for experimental contract work was of a temporary nature and fixtures for assembly were made of wood, very little of which had any useful value for later production. All excess costs on experimental contracts were classified as experimental and development expense. Such costs were accumulated from year to year during the performance of the several experimental contracts. No segregation of these costs was made as to their application to the specific contracts on which excessive costs were incurred, except the first amount deferred in 1938, which resulted from work on the experimental contract for the Airacobra.

The plaintiff deferred and capitalized as experimental and development costs the amount by which its total costs exceeded the experimental contract prices, as follows:

December 31, 1938	$ 128,052.77
December 31, 1939	511,776.21
December 31, 1940	888,931.68
Total	$1,528,760.66

93 Although the deferred experimental and development costs were not segregated in the plaintiff's accounts in respect to the specific contracts under which excess costs were incurred, the plaintiff's auditors arrived at an approximate allocation by deducting from the costs of fulfilling the contracts, the income received, as follows:

Airacudas	$ 889,499.48
Airacobra	229,086.30
Airabonita	410,174.88
Total	$1,528,760.66

The defendant's Army Audit Agency disallowed items totaling $29,021.43 (which disallowance is not involved in this dispute), leaving a balance of $1,499,739.23 in the deferred account for experimental and development expense, which sum represented the plaintiff's costs over and above the sums received under the contracts for experimental airplanes.

7. The plaintiff received no production contracts for any of the types described as Airacudas or the Airabonita airplanes. It received many contracts for great numbers of the Airacobra pursuit fighter plane, known as the P-39.

PRODUCTION TOOLING COSTS DEFERRED

8. April 26, 1939, the plaintiff entered into contract W 535 ac-12635 with the Army Air Corps for the delivery of 13 service test models of the Airacobra with additional parts at a fixed price of $1,073,445. Twelve of these planes were described as YP-39, Model 4-C, and one YP-39A, Model 4-D.

The work under this contract was merged in the shop with production on later contracts, and any additional experimental costs in connection with its performance were absorbed in the production costs on fixed-price production contracts.

Thereafter, from time to time, the plaintiff was awarded additional production contracts for P-39 Airacobras with both the United States and the British Governments. The earlier production contracts were fixed price, and the later ones were cost-plus-fixed-fee contracts. Under the cost-plus-fixed-fee contracts,
94 hereinafter referred to as CPFF contracts, the plaintiff was reimbursed for allowable costs of manufacture and was paid a fixed fee specified in the contract.

The production of P-39 Airacobras was continued on all of these contracts until April 1944, at which time the uncompleted contracts were amended to provide for deliveries of P-63 models. Numerous changes were made during the entire production period of the

P-39 models to reduce costs and facilitate production, to avoid field breakage and to improve functional operations.

9. The plaintiff received the following fixed-price contracts for the production and delivery of Airacobra fighter planes:

Item	Date of contract	Contract numbers	Unit planes and equivalent in spare parts	Models	Contract price
United States					
(E).....	4/26/39	W 535 ac-12635	13 1	YP-39 YP-39A	$1,073,445.00
(F).....	9/30/39	W 535 ac-13383	87	P-39C	2,833,236.00
(G).....	9/ 7/40	W 535 ac-15675 Increased	120 565	P-39D	4,962,220.00 21,276,912.79
(H).....	6/ 5/41	W 535 ac-32	180	P-39D-1	7,407,540.00
			966		$37,553,353.79
British					
	8/15/40	A-218	200	P-400	$9,517,507.55
	10/ 8/40	A-1326	250	P-400	9,647,163.33
	10/10/40	A-1476	360	P-400	14,645,980.19
Totals			810		$33,810,651.07
			1,776		$71,364,004.86

The United States contracts were entered into with the Army Air Corps.

The Model P-400 produced under British contracts was the British version of the P-39 and was of similar type and character as the Airacobra pursuit fighter planes specified under the contracts with the United States Army Air Corps.

The Army Air Corps contracts contain similar provisions, in respect to the right and license of the Government in any and all discoveries, inventions and improvements, as those set forth in Finding 4 for experimental contracts. These contracts also contain provisions substantially as follows:

95 *Provisions Reference Section 14 of the Act approved April 3, 1939—Limitation on Profits—It is expressly understood and agreed by both parties hereto that the contractor hereby agrees:*

• • • • •

(e) That the manufacturing spaces and books of its own plants, affiliates, and subdivisions shall at all times be subject to inspection and audit by any person designated by the Secretary of War, the Secretary of the Treasury and/or by a duly authorized committee of Congress.

• • • • •

Cost Records.—The contractor agrees to keep cost records in accordance with its own methods and practices of computing

costs of all expenses incurred by it in connection with the performance of this contract and such records shall be available for inspection of the Contracting Officer or his representative after the completion or earlier termination of this contract. Such cost data shall be for the information of the Government, but shall in no way affect the contract price of the articles, spare parts, supplies or work covered by this contract.

10. About April 1939, when the plaintiff received its contract for the production of service test models of the P-39 Airacobra, it began to fabricate and install permanent tooling for the production of this type of airplane. Production tooling is distinguished from ordinary machine tools, in that the latter are more permanent and universal in character, consisting of milling machines, lathes, drill presses, etc., not restricted in use to specific models or types of the product manufactured.

Production tooling for the P-39 pursuit fighter plane was largely assembly tooling, consisting of long-beam assembly, subassembly and tail-assembly fixtures, all of which were fabricated in structural steel and remained in use as long as this type of plane was in production. It also included metal tubes, angles, form blocks, jigs, router templets and templet dies. In the production of experimental models, most of these fixtures were fabricated in wood, and tooling was provided for temprorary use. But, in the production of service planes the plaintiff was required to provide for interchangeability of certain parts, such as wings, tails, and sur-
96 face landing gear, necessitating accurate duplications of the various parts.

As additional contracts for Airacobras were received during 1939 and 1940, the plaintiff increased its numbers of assemblies to provide for greater production and duplicated the tooling for such assemblies, subassemblies, and such auxiliary tooling as became necessary to meet increased production requirements. The plaintiff provided tooling for its Niagara Falls plant, which started operations in June 1941, similar to that it had installed in its Elmwood Avenue plant.

During 1939 and 1940, the plaintiff incurred costs for production tooling for the P-39 Airacobra in the sum of $1,894,109.57. In December 1940, the plaintiff recorded this sum in a deferred account, together with the deferred costs on experimental contracts, entitled "Experimental, Development and Production Tooling Expenses." The defendant's Army Audit Agency disallowed $19,383.80 of the deferred cost for tooling, leaving $1,874,725.77 for allocation to future production.

11. In addition to the special production tooling set forth in the preceding finding, a substantial amount of additional tooling was required in the fabrication of P-39 airplanes.

The plaintiff's estimated tool charges for the various fixed-price contracts, other than the deferred costs, totaled $2,597,435.40. Its actual tooling costs for fixed-price production, other than the deferred tooling, were $2,233,239.47.

Some of the tools which had been provided as a preliminary to production and deferred for allocations against future production, would become worn out by use or obsolete as a result of current changes in design. Some were reworked and others were scrapped and replaced. The costs of reworking or replacing original tooling would be charged against current production and would be included in the tool costs in the preceding paragraph.

12. In connection with plaintiff's quotations on each of the fixed-price contracts (Finding 9), except the last two British contracts, plaintiff submitted a breakdown of its estimated costs of production. At that time only a portion of the experimental and development costs had been determined and set up in the deferred
97 account. Likewise, the production tooling expense involved herein had not yet been determined or set up in the deferred account inasmuch as that expense grew largely out of the performance of the fixed-price contracts. Accordingly, the cost estimates submitted in connection with each of plaintiff's fixed-price contracts in 1939 and 1940 did not contain any provision for the amortization of any part of the deferred experimental development and production tooling costs.

AMORTIZATION OF EXPERIMENTAL, DEVELOPMENT AND PRODUCTION TOOLING EXPENSE

13. As of December 31, 1940, the plaintiff had capitalized and deferred experimental, development and production tooling expense, as follows:

	Amounts expended and deferred by plaintiff	Disallowed by Army Audit	Net amounts subject to amortization
Experimental and development expense (Finding 6)	$1,528,760.66	$29,021.43	$1,499,739.23
Production tooling for P-39's (Finding 10)	1,894,109.57	19,383.80	1,874,725.77
Total	$3,422,870.23	$48,405.23	$3,374,465.00

14. The plaintiff originally planned to amortize its deferred costs of $3,374,465 on the basis of the number of planes delivered and to be delivered on all production contracts on hand at the end

of each year, and by prorating such costs annually against deliveries made during the current year.

Under the aforesaid plan the amount of amortization applicable to each airplane produced and delivered would decrease from year to year in proportion to the total increase in the number of planes under contract at the end of each year. At the end of the year 1940, the plaintiff had contracted to deliver approximately 1600 airplanes under its fixed-price contracts.

15. During 1941, the plaintiff received an additional fixed-price contract W 535 ac-32 for 180 planes and equivalent in parts. This contract appears in the table of fixed-price contracts, Finding 9.

In the latter part of the same year, the plaintiff entered into
98 two cost-plus-fixed-fee contracts for 2,392 airplanes of a similar type. According to the plan of amortization above referred to, a portion of the deferred experimental, development, and production tooling costs would have been allocated to planes produced and delivered under these CPFF contracts. However, plaintiff's officials had been advised by Army Air Force officials that the deferred expenses in question might not be approved for reimbursement under the CPFF contracts being negotiated. In order to avoid any question of allowable reimbursements, plaintiff changed its original plan of amortization by limiting the allocation of the deferred charges to its fixed-price production contracts only. Accordingly, plaintiff added only the additional planes covered by the fixed-price contract entered into in 1941, and the amounts charged to each plane thereafter remained constant.

16. The plaintiff's annual reports which were prepared and certified to by Price, Waterhouse & Company, certified public accountants, contain the following explanatory comments regarding the treatment of experimental, development and production tooling costs:

ANNUAL REPORT FOR 1938

> The company, from its inception, has charged currently to costs of contracts in progress all experimental and development work as the contracts were completed. During the year 1938 substantial experimental and development work of basic future value to the company was accomplished in connection with a contract for the design and construction of an experimental airplane. The total expenditures, including the costs for basic development above referred to, charged to the costs of such contract, plus the estimated costs to complete, amounted to $128,052.77 over and above the contract price of the experimental plane. The sum of $128,052.77 was transferred to a deferred account at December 31, 1938.

ANNUAL REPORT FOR 1939

C—The deferred experimental and development expenses were in respect of two experimental airplanes.

The first of these (known as the Airacuda) was practically completed at December 31, 1937, and the estimated excess
99 of its cost over the contract sales price was charged to profit and loss accounts for the year 1937. Subsequent to the delivery of the airplane in 1938 expenditures were made in connection with improvements in design and in further development of this project. Such additional expenditures, amounting to $200,320.23 have been deferred at December 31, 1939, as, in the opinion of the management, the development of this type of airplane has a probable value to the Company in connection with expected future sales. A contract for 13 Airacudas for service test involving three experimental variations of the original Airacuda, now in progress, is expected to be completed during 1940. Since the date of closing the annual accounts the Company has made substantial expenditures, not theretofore anticipated, in connection with the contract for thirteen Airacudas. The amount of the total excess costs over the contract price has not been determined at this time.

The second of the experimental airplanes is being constructed for the Navy and the amount of $217,682.92 deferred in respect of this airplane is the excess of the estimated total cost when completed over the contract sales price. In the opinion of the management, such excess costs constitute development and experimental expenditures of value in connection with expected orders for this or similar types of aircraft.

The amount of $128,052.77 deferred at December 31, 1938, in respect of another experimental airplane has now been transferred to costs of airplanes of similar type for which contracts were received in 1939; accordingly the amount deferred at December 31, 1938, is included in the inventory of work in progress at December 31, 1939.

It is the Company's intention to charge the deferred experimental and development expenses to costs of future production (exclusive of the service test order above referred to) or, if and when the projects are abandoned, to charge them off to profit and loss accounts.

ANNUAL REPORT FOR 1940

During the past five years, the Company has developed three types of Airplanes known as Airacobra, Airacuda, and Airabonita, all three incorporating certain similar basic new developments. In the opinion of the management the excess costs

on experimental and service test contracts constitute experimental and development charges and, together with costs of tooling for production, have been deferred. Such costs amounted, in the aggregate, to $3,422,870.23 at December 31, 1940 and consisted of charges on the Airacobra of
100 $2,123,195.87, on the Airacuda of $889,499.48 and on the Airabonita of $410,174.88. The Company is at present concentrating on the manufacture of Airacobras, and it is the Company's intention to absorb the aggregate of the foregoing charges on the basis of the quantities of this model under contract. Amortization amounting to $70,773.45 has been charged against cost of goods sold in 1940.

ANNUAL REPORT FOR 1941

Experimental, development and production tooling expenditures amounting to $3,352,096.78 were deferred at December 31, 1940, to be absorbed on the basis of certain quantities of aircraft under contract. Of this amount an amortization of $1,998,184.02 applicable to aircraft delivered during 1941 was charged to cost of goods sold for that year.

During 1942, the plaintiff amortized the remaining experimental, development and production tooling costs in its deferred account against deliveries of airplanes under its fixed-price contracts.

17. Thus at the end of 1942, the plaintiff had amortized its entire deferred costs for experimental, development and production tooling against deliveries under its fixed-price contracts, as follows:

Contract number	1940	1941	1942	Totals
United States				
W 535 ac-12635	$27,880.45	$ 1,923.18	.....	$ 29,803.63
W 535 ac-13383	42,893.00	128,853.06	.....	171,746.06
W 535 ac-15675	.....	934,665.48	$382,712.82	1,317,378.30
W 535 ac-32	.....	.....	346,172.40	346,172.40
Totals	$70,773.45	$1,065,441.72	$ 728,885.22	$1,865,100.39
British				
A-218	.....	$ 369,250.56	$ 15,385.44	$ 384,636.00
A-1326	.....	405,790.98	75,004.02	480,795.00
A-1476	.....	157,700.76	534,638.08	692,338.94
Totals	.....	$ 932,742.30	$ 625,027.54	$1,557,769.94
Totals	$70,773.45	$1,998,184.02	$1,353,912.76	$3,422,870.23

COST-PLUS-FIXED-FEE CONTRACTS

18. In the meantime, commencing August 14, 1941, the plaintiff had entered into a series of cost-plus-fixed-fee, or CPFF, contracts with the defendant through the United States Army Air Corps for the production of P-39 or Airacobra airplanes.

101 Under the CPFF contracts the defendant agreed to reimburse the plaintiff for the cost of manufacturing and in addition to pay the plaintiff a fixed fee as provided in each of such contracts. The particular contracts, with dates of execution, are described in the following table:

Item	Date of contract	Contract numbers	Airplanes and equivalent in spare parts	Type	Estimated costs	Fixed fee specified
(I)...	8/14/41	W 535 ac-20910..	1,980	P-39D ...	$ 70,960,740	$ 4,257,644.40
(J)...	9/10/41	DA W 535 ac-156	412	P-39D-1 ..	14,985,926	899,155.56
(K)..	6/29/42	W 535 ac-29318..	2,700	P-39E	88,670,000	3,546,800.00
	4/13/45	Increase	2,470	P-63A-1 ..	64,814,800	2,592,592.00
(L)...	9/28/43	W 535 ac-40071..	2,600	P-39Q	68,387,200	2,735,488.00
Totals.....			10,162	.....	$307,818,666	$14,031,679.96

By supplemental agreement dated September 29, 1942, contract W 535 ac-29318 was changed to provide for deliveries of Model P-63A-1 in lieu of the P-39 type specified under the original contract. Contract W 535 ac-40041, dated January 5, 1944, for 2,470 planes and equivalent in spare parts, type P-63A-1, was combined on April 13, 1945, and made a part of contract W 535 ac-29318 and is represented by the increase as noted in the above table.

The production of P-39 models was discontinued in April 1944 on all of the above-described contracts and changed over to P-63 models on which production was thereafter continued.

Deliveries were completed under contract DA W 535 ac-156, W 535 ac-40071 was terminated November 3, 1944, and contracts W 535 ac-20910 and W 535 ac-29318 were terminated for the convenience of the Government August 14, 1945. Termination settlement agreements were consummated pursuant to the Contract Settlement Act of 1944.

19. Each of the CPFF contracts contains the following provisions:

ARTICLE 3. CONSIDERATION

(a) The Government will pay the Contractor upon satisfactory delivery of all items specified in the Contract, subject to reimbursement for cost, as outlined in Article 6 hereof, the cost, plus a fixed fee of * * * being * * * percent of the total
102 estimated cost of * * *. This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof. Provided, however, that there shall be no adjustment in the amount of

the fixed-fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost of the work or where the estimated cost varies from the actual cost.

(b) For the purpose of determining the amount payable under this Contract, allowable items of cost will be determined by the Contracting Officer in accordance with Regulations for determination of the cost of performing a Contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. It being understood and agreed without limiting the generality of the foregoing, that

(1) All costs which have been incurred by the Contractor in anticipation of this Contract and prior to the signing thereof, and which if incurred after the signing of this Contract, would have been considered as allowable items of cost within the meaning of said Regulations, shall be considered as allowable items of cost incurred hereunder.

Article 3 (b) (2) of contracts W 535 ac–20910 and DA W 535 ac–156, and Article 3 (d) of contracts W 535 ac–29318 and W 535 ac–40071, provide:

(2) Any cost incurred by the Contractor under the terms of this Contract which would constitute an allowable item of cost under the provisions of paragraph (b) of this Article shall be included in determining the amount payable under this Contract, notwithstanding any provisions contained in the specifications or other documents incorporated in this Contract by reference, designating services to be performed or materials to be furnished by the Contractor at its epense or without cost to the Government.

Section 26.9 of Chapter 1 of Title 26, Code of Federal Regulations, as contained in T. D. 5000, is a promulgation of regulations governing the computation of Excess Profits Taxes, and provides, in part, as follows:

103 *Cost of performing a contract or subcontract*—(a) *General rule.*—The cost of performing a particular contract or subcontract shall be the sum of (1) the direct costs, including therein expenditures for materials, direct labor and direct expenses, incurred by the contracting party in performing the contract or subcontract, and (2) the proper proportion of any

indirect costs (including therein a reasonable proportion of management expenses) incident to and necessary for the performance of the contract or subcontract.

• • • • •

(e) *Factory cost.* • • •

(5) *Indirect factory expenses.*—Items, usually termed "factory overhead," which are not directly chargeable to the factory cost of performing the contract or subcontract but which are properly incident to and necessary for the performance of the contract or subcontract and consist of the following:

• • • • •

(D) *Fixed charges and obsolescence.*—Recurring charges with respect to property used for manufacturing purposes of the contract or subcontract, such as premiums for fire and elevator insurance, property taxes, rentals and allowances for depreciation of such property, including maintenance and depreciation of reasonable standby equipment; and depreciation and obsolescence of special equipment and facilities necessarily acquired primarily for the performance of the contract or subcontract, except special additional equipment and facilities with respect to which the Secretary of the Department concerned has made a certification binding upon the Commissioner of Internal Revenue, • • •

(d) *Other manufacturing cost.*—Other manufacturing cost as used in paragraph (b) of this section includes items of manufacturing costs which are not properly or satisfactorily chargeable to factory costs (see paragraph (c) of this section) but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, payments of royalties and amortization of the cost of designs purchased and patent rights over their useful life; and "deferred" or "unliquidated" experimental and development charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current
104 charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. In the case of general experimental and development expenses which may be charged off currently, a reasonable portion thereof may be allocated to the cost of performing the contract or subcontract. If a special experimental or development project is

carried on in pursuance of a contract, or in anticipation of a contract which is later entered into, and the expense is not treated as a part of general experimental and development expenses or is not otherwise allowed as a cost of performing the contract, there clearly appearing no reasonable prospect of an additional contract for the type of article involved, the entire cost of such project may be allowed as a part of the cost of performing the contract.

Said Section 26.9 of T. D. 5000 further provides in subparagraph (g) (4) thereof as follows:

• • • Among the items which shall not be included as a part of the cost of performing a contract or subcontract or considered in determining such cost, are the following: • • • losses on the other contracts; • • •

20. CPFF contracts W 535 ac-20910, DA W 535 ac-156, and W 535 ac-29318, provide in Articles 6, 16, and 17 (a) thereof as follows:

ARTICLE 6. PAYMENTS

(a) *Reimbursement for Cost.*—The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 hereof as may be approved or ratified by the Contracting Officer, and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers; • • •

ARTICLE 16. DISPUTES

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact arising under this contract shall be decided by the Contracting Officer, subject to written appeal by the Contractor within 30 days to the head of the department concerned or his duly authorized representative, whose decision shall be final and conclusive upon the parties hereto. In the meantime the Contractor shall diligently proceed with performance.

105 ARTICLE 17. DEFINITIONS

(a) The term "head of the department" as used herein shall mean the head or any assistant head of the executive department or independent establishment involved, and the term "his duly authorized representative" shall mean any person authorized to act for him other than the Contracting Officer.

CPFF contract W 535 ac–40071 provides in Article 16 thereof, as follows:

ARTICLE 16. DISPUTES

Except as otherwise specifically provided in this contract, all disputes concerning questions of fact which may arise under this contract, and which are not disposed of by mutual agreement, shall be decided by the Contracting Officer, who shall reduce his decision to writing and mail a copy thereof to the Contractor at his address shown herein. Within 30 days from said mailing the Contractor may appeal in writing to the Secretary of War, whose written decision or that of his designated representative or representatives thereon shall be final and conclusive upon the parties hereto. The Secretary of War may, in his discretion, designate an individual, or individuals, other than the Contracting Officer, or a board as his authorized representative to determine appeals under this Article. * * * Pending decision of a dispute hereunder the Contractor shall diligently proceed with the performance of this contract. Any sum or sums allowed to the Contractor under the provisions of this Article shall be paid by the United States as part of the cost of the articles or work herein contracted for and shall be deemed to be within the contemplation of this contract.

REALLOCATION OF DEFERRED COSTS TO ALL PRODUCTION CONTRACTS

21. In 1942, at which time the plaintiff was engaged in production on CPFF contracts described in Finding 18, the Internal Revenue Bureau of the Treasury Department required that, for income tax purposes, the experimental, development and production tooling expenses should be allocated to airplanes produced under CPFF contracts as well as the fixed-price contracts.

106 A copy of a memorandum by Paul C. Gillette, Engineer Revenue Agent, dated March 12, 1942, in reference to the plaintiff's operations for the years 1939 and 1940, was furnished to the plaintiff. It contained the following recommendation:

That the entire costs at December 31, 1940, in the Development and Jig Expense Account, including the losses incurred, not charged off in prior years, on the Airacuda and Airabonita models, be amortized at a rate represented by the ratio of planes produced during the year compared with the total of planes produced and on order at the end of the year.

This recommendation was in harmony with the plaintiff's original plan of amortization.

The plaintiff declined to accept this recommendation and continued to amortize the remaining deferred charges for experimental,

development, and production tooling costs against the deliveries of airplanes under its fixed-price contracts during the remaining months of 1942, as set forth in Finding 17. The Bureau of Internal Revenue, however, adjusted the plaintiff's income for 1941 and 1942 for amortization by allocating such costs to deliveries under fixed-price contracts and deliveries made and to be made under CPFF contracts. Additional taxes assessed and paid for 1941 and 1942 totaled approximately $1,337,474.89.

22. On September 19, 1942, Charles L. Beard, then Secretary and Treasurer of the plaintiff corporation in a memorandum directed to John Berry, Jr., Comptroller of the plaintiff corporation, made *inter alia* the following statement of policy in connection with such deferred experimental, development and production tooling expenses as it related to the above-mentioned suggestion then being made by the Bureau of Internal Revenue:

> This item should be allowed as an amortization expense against the fixed price contracts only in view of the fact that any amortization to be allowable under a cost-plus-fixed-fee contract would have to be included in the original negotiations of such contract. No provision is made for that on any of our cost plus contracts in view of the position taken by the Government that prior to our entry into cost plus contracts we have received sufficient fixed price contracts to permit the amortization of deferred experimental expenses.

107 On April 2, 1943, John Berry, Jr., prepared and submitted to the Resident Auditor, Army Air Forces, a "Statement of Accounting Policies, Pertinent to Operations Under Cost-Plus-A-Fixed-Fee Supply Contracts," in which he made the following statement in connection with deferred charges for experimental development and production tooling expense:

> 3. Deferred Charges.—
>
> • • • • •
>
> (c) Experimental, development and production tooling expenses are written off against the deliveries of the items to which expenditures apply. No experimental expense is charged to overhead applicable to CPFF contracts. • • •

23. On September 7, 1943, the plaintiff wrote to the Price Adjustment Board, War Department, New York City, an outline of its proposed future amortization of said deferred charges. Major Knox B. Phagan was at that time Army Air Corps Price Adjustment Officer. Said letter is as follows:

> Pursuant to our telephone conversation this afternoon, we should be glad if you would indicate your approval of the

method to be followed in amortizing development and experimental expenses and production tooling costs of P–39 airplanes.

Our records as of December 31, 1942, and the schedules originally submitted to you showed that we had amortized the full amount of these costs against fixed price contracts. You objected to such treatment on the ground that the costs should be amortized over cost plus a fixed fee as well as fixed price contracts. The Bureau of Internal Revenue in examining our Federal income and excess profits tax return for the calendar year 1941 had made the same objection and required us to amortize the costs over all airplane contracts then held by us. In view of the position taken by the Bureau of Internal Revenue and yourselves we have agreed to amortize the experimental and development expenditures over all contracts for P–39 and P–63 airplanes and the P–39 production tooling expenditures over all contracts for P–39 airplanes, provided that the amounts disallowed by you against fixed price contracts become items of reimbursable costs under our cost plus a fixed fee contracts and are allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office.

108 Under date of August 14, 1943 we provided you with two schedules which set forth in detail the amounts and contracts involved in the write-off from January 1, 1940, to June 30, 1943, on an actual write-off basis and through the balance of 1943 and 1944 on an estimated basis.

The method agreed upon involved a determination of each of the two amounts involved, which amounts are as shown by our books (and less adjustments aggregating $2,892.19 are as shown by a report of an Agent of the Bureau of Internal Revenue as of December 31, 1940) less adjustments made by the Contract Audit Section of the Army Air Forces as a result of their examination of the costs. The amounts are as follows:

	Development and experimental	P–39 production tooling	Together
Costs to December 31, 1940 (There were no additions subsequently)	$1,528,760.66	$1,894,109.57	$3,422,870.23
Less—Costs disallowed by Contract Audit Section, Army Air Forces	29,021.43	19,383.80	48,405.23
Amount to be amortized as agreed upon with Price Adjustment Board and Contract Audit Section, Army Air Forces	1,499,739.23	1,874,725.77	3,374,465.00

The last amounts shown above are to be amortized over all fixed price and cost plus a fixed fee supply contracts for P–39 and P–63 airplanes as follows:

The sum of the number of airplanes and equivalents on order and undelivered at the beginning of the year and the number of airplanes and equivalents ordered during the calendar year is to be divided into the unamortized cost as of the beginning of the year, the resulting quotient represents the amortization per airplane. The amortization per airplane multiplied by the number of airplanes and equivalents accepted by the Army Air Forces during the period for each contract results in the amortization per contract.

We believe the foregoing sets forth the understanding between us as to the amortization of the expenditures for experimental and development and P–39 production tooling and if it is in accordance with your understanding we should like you to so indicate by signing one copy of this letter and returning it to us.

Yours very truly,

BELL AIRCRAFT CORPORATION,
(Signed) JOHN BERRY, JR.,
Comptroller.

109 The explanation and method of amortization set forth in this letter is in accordance with our understanding and has our approval.

(Signed) KNOX B. PHAGAN,
Maj. A. C., Price Adj. Officer.

Date: Sept. 9, '43.

The plan of amortization outlined in the above letter is in accordance with the decision of the Internal Revenue Bureau. It was the plaintiff's original plan of amortizing these costs against production under fixed-price contracts before it had received any of its CPFF contracts. Major Phagan was then Chief of the Price Adjustment Section, Eastern District, Air Forces.

24. On September 9, 1943, the plaintiff's comptroller issued instructions for the restoration to the deferred account the proportion of experimental, development and production tooling which became applicable to airplanes delivered and to be delivered under the CPFF contracts, in accordance with the approved plan of reamortization. There was restored the sum of $2,286,819.95, consisting of:

Experimental and development costs	$1,035,918.73
Production tooling for P-39 planes	1,250,901.22

The unrestored difference of $1,087,645.05 previously amortized represented that portion of experimental, development and pro-

duction tooling which was applicable to deliveries under the fixed-price contracts in accordance with the approved plan of reamortization.

Reimbursement vouchers were prepared by the plaintiff and submitted in the sum of $451,179.96 for reallocation of amortization of experimental, development, and production tooling on deliveries under CPFF contracts during 1942 and $848,676.06 for deliveries under CPFF contracts during January to August, inclusive, of 1943, as follows:

Contract numbers	Experimental and development expenses	Production tooling costs	Total
W 535 ac-20910	$370,552.30	$819,571.64	$1,190,123.94
DA W 535 ac-156	37,318.96	72,413.12	109,732.08
Total	407,871.26	891,984.76	1,299,856.02

Defendant's Assistant Resident Auditor, Mr. DiLapo, considered the vouchers and recommended to the Resident Auditor, Mr.
110 Campbell, that they be rejected as not constituting costs allowable under the contract for the following reasons: that in the period prior to the inception of plaintiff's CPFF contracts, the contractor had followed a consistent policy of charging off all of these experimental, development, and production tooling expenses against its fixed-price contracts which were then in effect; that in the opinion of the assistant auditor there was no provision in the CPFF contracts for the re-imbursement to a contractor of *losses* suffered under fixed-price contracts and that these particular expenses were losses suffered by Bell in the performance of its fixed-price experimental contracts in 1936-1938. Mr. Campbell, the resident Auditor, did not agree with this position, and certified the vouchers to the Contracting Officer. The defendant's Contracting Officer approved the above vouchers for reimbursement under the CPFF contracts, and the plaintiff was paid the said sums by the defendant's Finance Officer.

25. Commencing in October 1943, the plaintiff submitted additional reimbursement vouchers for experimental, development, and tooling costs, representing the proportionate amounts applicable to deliveries subsequent to August 1943 under CPFF contrasts, as follows:

Contract numbers	Experimental and development expenses	Production tooling costs	Total
W 535 ac-20910	$194,947.81	$79,991.20	$274,939.01
DA W 535 ac-156	13,888.85	4,371.50	18,260.35
W 535 ac-29318	223,288.09	69,895.04	293,183.13
W 535 ac-40071	195,922.72	204,658.72	400,581.44
Total	628,047.47	358,916.46	986,963.93

The above sums represent vouchers for all of the remaining experimental, development, and production tooling costs for which the plaintiff claimed reimbursement. No part of these sums has been paid.

26. As these vouchers began to arrive for audit in October 1943 the defendant's Resident Auditor, Roland Campbell, had been replaced by Frank Ferris. About the same time, Bancroft Mitchell, the Contracting Officer for the plaintiff's CPFF contracts, was replaced by Maj. Harold B. Davies, who acted both as Ad-
111 ministrative Contracting Officer and Termination Contracting Officer.

The Assistant to the Resident Auditor, James D. DiLapo, again recommended against approval of these vouchers for reimbursement on the ground that the plaintiff had consistently charged its experimental, development and production tooling costs against deliveries under its fixed-price contracts, and for the further reason that DiLapo considered such costs as losses on other fixed-price experimental contracts which would not be reimbursable costs under CPFF contracts. Approval of these vouchers was withheld by Ferris.

In February 1944, the defendant's Resident Auditor Ferris was replaced by one Harry Leibman, who likewise withheld approval of these vouchers on the ground that the CPFF contracts contained no provision for payment of experimental, development and production tooling expenses, except by reference to T. D. 5000, and for the further reason that the plaintiff had previously amortized such costs against fixed-price contracts.

Major Davies declined to approve these vouchers, since these deferred costs had been previously amortized against deliveries under fixed-price contracts, and he thought the plaintiff had changed its method for the reamortization of such costs over all contracts as a result of the decision of the Bureau of Internal Revenue, but without the approval of the Contracting Officer.

27. In April and May 1944, the Chief Cost Auditor for the General Accounting Office, Buffalo area, submitted to the Resident Auditor a series of "informal inquiries" in respect to the reimbursements of experimental, development and production tooling costs by Col. J. Harris, Finance Officer, in August and September 1943, summarized in Finding 24, as follows:

		Reimbursement exceptions	
Informal inquiry	Dated	Contract	Total payments
777	4/25/44	W 535 ac-20910	$1,064,888.18
778	4/25/44	DA W 535 ac-156	109,732.08
789	5/13/44	W 535 ac-20910	125,235.76
Total (Finding 23)			1,299,856.02

112 Each of the foregoing inquiries made exception to such payments as follows:

Since the entire amount of the Deferred Experimental and Development Expenses and the Production Tool Expenses were amortized or written off against prior commercial and Government fixed price contracts by the contractor, the status of the account at the time of the negotiations with respect to the estimated costs under his contract was such as to preclude consideration thereof as an existing "Deferred" or "unliquidated" charge to the contract and the fact that for tax purposes the account was reopened and amortized in part against this contract would appear to afford no proper basis for considering the amount so amortized as a reimbursable item of cost under this contract.

28. By letters dated June 29, 1944, the Resident Auditor, Harry Leibman, advised the Chief Cost Auditor for the General Accounting Office at Buffalo that deductions were made on vouchers listed in the said letters to recover payments for experimental, development and production tooling costs, in accordance with informal inquiries 777, 778 and 789. Copies of these letters were furnished the plaintiff.

The Contracting Officer held up the vouchers on which the Resident Auditor made deductions, and took no action upon them until September 1944.

In the interim the Comptroller General of the United States issued formal notices of exception and suspensions of the accounts of Colonel J. Harris, Finance Officer at Buffalo, dated August 18, 1944. These notices covered the sums of $1,064,888.18 and $109,732.08, on which exceptions were noted by informal inquiries Nos. 777 and 778 and for the same reason. They were received by the Finance Officer August 21, 1944. Recoupment of these sums was made immediately by the Finance Officer on vouchers for monies otherwise due the plaintiff, and the Comptroller General was advised thereof by reply endorsements August 25, 1944.

On September 6 and 8, 1944, the Contracting Officer transmitted to the Finance Officer for settlement, groups of the plaintiff's vouchers, which included the vouchers on which deductions were made by the Resident Auditor, as above. The Contracting Officer reinstated vouchers for $1,064,888.18 and $109,732.08 for which sums had been recovered by the Finance Officer, but other
113 deductions for $125,235.76 were approved by him in compliance with informal inquiry and exception No. 789, and in harmony with the formal notices of exception and suspension previously received by the Finance Officer.

On September 12, 1944, the Finance Officer received a formal notice of suspension from the Comptroller General dated September 11th for the sum of $125,235.76, in accordance with informal inquiry No. 789. A reply endorsement was issued the following day by the Finance Officer for removal of the suspension since this sum had been deducted from vouchers for amounts otherwise due the plaintiff. Thus the payments totaling $1,299,856.02 for experimental, development and production tooling costs reimbursed to the plaintiff on CPFF contracts were fully recovered by the defendant.

29. Experimental, development, and production tooling costs which were amortized and vouchered for reimbursement by the plaintiff under CPFF contracts, Findings 24 and 25, are combined as follows:

Contract number	Experimental and development expense	Production tooling costs	Total
W 535 ac-20910	$565,500.11	$899,562.84	$1,465,062.95
DA W 535 ac-156	51,207.81	76,784.62	127,992.43
W 535 ac-29318	223,288.09	69,895.04	293,183.13
W 535 ac-40071	195,922.72	204,658.72	400,581.44
Total	1,035,918.73	1,250,901.22	2,286,819.95

30. The second Contracting Officer declined to approve the additional vouchers for $986,963.93 (Findings 25 and 26), and on January 10, 1945, he wrote to plaintiff stating that he was forwarding a copy of a decision by the Chief of the Procurement Division, which decision the Contracting Officer stated he was adopting as his findings of fact and decision in denying reimbursement to the contractor for the expenditure as requested on a covering list of Audit Bureau Vouchers. The enclosed decision of the Chief of the Procurement Division was dated November 13, 1944, and was apparently in response to a request for advice originating in a letter of December 10, 1943, from the Resident Auditor on the Bell project, forwarded under a subject heading reading
114 "Amortization of Losses on Fixed Price Contracts". The decision discussed generally the handling by Bell of the entire amount of experimental, development, and production tooling exepnses carried in the deferred account. It took the position that the profits earned by Bell on its *fixed price* production contracts were "more than enough to recover for Bell Aircraft Corporation the total amount of the expenditures of $3,422,870.23 • • • and were so treated on the books of Bell Aircraft Corporation"; that Bell had failed to show that it had not in fact recovered through the fixed-price production contracts the entire amount of such development expenses; that the $2,286,819.95 which Bell had

charged on its books against CPFF contracts did not, in fact, represent costs of performing such CPFF contracts, and that reimbursement for such costs under the CPFF contracts would result in Bell's receiving double payment from the Government. The letter concluded:

> It is therefore the opinion of this Headquarters that Bell is not entitled to reimbursement under its CPFF contracts for P–39 and P–63 airplanes for any portion of the said sum of $2,286.819.95.

On March 1, 1945, the second Contracting Officer wrote to plaintiff again stating that the findings of fact and decision which he had rendered on January 10, 1945, were rescinded and new findings and decision were forwarded. The new findings listed the same unpaid vouchers, and continued almost word for word in the same manner as the previous communication of January 10, except for the omission of the first paragraph which had related the circumstances under which the Chief of Procurement was rendering advice, and a change in the last paragraph of the "findings" so that it read , "It is, therefore, the decision of the Contracting Officer" rather than, "It is therefore the opinion of this Headquarters."

The sum of $2,286,819.95 mentioned in both sets of findings represents the $1,299,856.02 which had been approved by the predecessor Contracting Officer, paid, and recouped by the Finance Officer under suspension by the Comptroller General, as well as the unpaid vouchers totaling $986,963.93, summarized in Finding 25,
115 for which no payment had been made.

31. On March 27, 1945, the plaintiff made timely appeal from the findings and decision of the second Contracting Officer, in denying payment on vouchers totaling $986,963.93. The sum of $1,299,856.02, which had been previously reimbursed and was noted for exception and suspension of the accounts of the Finance Officer by the Comptroller General, was not appealed by the plaintiff nor considered by the War Department Board of Contract Appeals, representing the Secretary of War.

On April 29, 1946, the War Department Board of Contract Appeals rendered its decision on the plaintiff's appeal in which it denied the reimbursement of the said sum of $986,963.93. This decision states in part:

> All of the contracts contain a "Disputes" article and all of these articles except the one in Contract No. DA-W 535-ac-156 authorize the designation of a board as the representative of the Secretary of War to determine appeals from the decisions of the contracting officer. The mentioned contract provides

only for appeal to the head of the department or his duly authorized representative. Insofar as the questions presented by this appeal are questions of law they will be administratively determined pursuant to the memorandum of Secretary of War dated 4 July 1944.

There is no dispute between the parties as to the amount of the costs or as to the propriety of the method of allocation used by appellant. The only question presented is whether reimbursement for any portion of these costs is authorized or required by the subject contracts under the circumstances here involved. The subject contracts do not expressly provide for reimbursement of these costs but provide that allowable items of cost will be determined by the contracting officer in accordance with the provisions of T. D. 5000.

The experimental and development costs are clearly within the category of indirect costs as defined by T. D. 5000 and are specifically covered by Section 26.9 (d) of T. D. 5000—set out above. There is no specific reference in T. D. 5000 to the amortization of production tooling costs and appellant has not pointed out a specific provision of T. D. 5000 which it considers as providing for the allowance of such an item of cost. In the pamphlet issued by the War and Navy Departments
116 entitled "Explanation of Principles for Determination of Costs Under Government Contracts" (Par. 18), it is indicated that items such as royalties and the amortization of the initial cost of dies, patterns, and special tools can logically be classified as direct shop costs and be charged to contracts on an equitable basis of apportionment. Section 26.9 (e) (5) (D) of T. D. 5000 set out above also provides that charges for depreciation of property used in the manufacturing process may be treated as an item of cost. It is clear from the record and evidence that the production tooling was used in the performance of CPFF contracts calling for the production of the P-39 type of airplane. It would seem, therefore, that items of this type are within the intent and meaning of T. D. 5000.

• • • • •

Although it is true that costs of this type may properly be allowed as reimbursable items under T. D. 5000, it does not follow that such costs must be reimbursed under T. D. 5000 in all cases and under all circumstances. In order to determine whether such items of costs should be reimbursed it is necessary to examine all of the circumstances and facts involved. The subject costs—both engineering and development, and

production tooling costs—were incurred a considerable time before any of the CPFF contracts were entered into. The production tooling costs were incurred for the express and admitted purpose of performing certain fixed-price contracts then on hand or in process of negotiation. They were not incurred in anticipation of the CPFF contracts and would have necessarily been incurred regardless of whether any further contracts for the P-39 type of airplane were received or not. The engineering and development costs were incurred during the period 1938 to 1940 and the costs were capitalized because it was felt that the development in connection with which they were incurred had a probable value in connection with expected future sales. In 1940 appellant entered upon a course of conduct by which these costs were charged against certain fixed-price contracts. The procedure of charging these costs against fixed-price contracts was continued during 1941 and 1942 in accordance with the mentioned plan to the effect that at the end of 1942 all of the costs in question had been absorbed. During this period some of the subject CPFF contracts were entered into and all of them were negotiated prior to August of 1943 at which time appellant changed its plan of amortization to the one now contended for. It is clear from the record that no portion of these costs was in-
117 cluded in the estimates under the CPFF contracts and no specific consideration was given to the question of reimbursement in the negotiation of the subject contracts. It also may be reasonably concluded that appellant had no intention, at the time the contracts were entered into, of seeking reimbursement for such costs since its accounting method did not contemplate reimbursement.

* * * * *

Under these circumstances, it is difficult to understand how it can now be reasonably contended that an item of cost is reimbursable under the terms of the subject contracts, when, at the time the contracts were negotiated, appellant did not intend that the item should be reimbursable and was in fact charging the costs in question against other contracts in accordance with a previously adopted plan. The contracting officer in effect has found that the costs in question were in fact recovered by appellant through the fixed-price contracts. Although appellant states that these costs were not specifically set out as such in the quotations on the fixed-price contracts, it produced no evidence that these costs were not in fact recovered under the fixed-price contracts. Under the circum-

stances here present, the Board is of the opinion that the costs are not reimbursable under the subject contracts.

* * * * *

For the reasons herein set out the appeal insofar as it relates to contracts numbered W 535-ac-20910, W 535-ac-29318, W 535-ac-40071, and W 535-ac-40041 is denied.

In respect to contract DA W 535 ac-156, the President of the Board, the duly authorized representative of the Secretary of War, decided in accordance with the entire Board on other contracts, and denied the plaintiff's appeal insofar as it related to this contract.

The plaintiff's application for a rehearing was denied by the Board May 31, 1946.

32. Upon the termination of hostilities, plaintiff's CPFF contracts then in progress were terminated for the convenience of the Government. Termination settlement agreements were entered into pursuant to the Contract Settlement Act of 1944, in which plaintiff made reservations in respect to its claims for reimbursements under the CPFF contracts, as follows:

118 The Supplemental Settlement Agreement dated December 21, 1945, covering the termination of contract W 535 ac-20910, contains the following reservation in Article 4 (c) (2) (b):

> Claim for experimental and development and research costs in the amount of $1,465,062.95 which is now the subject of an appeal pending before the War Department Board of Contract Appeals.

The Supplemental Settlement Agreement dated May 15, 1946, covering the termination of contract W 535 ac-29318, contains the following reservation in Article 4 (c) (2) (b):

> $293,183.13 of experimental and development expenses now the subject of an appeal pending before the War Department Board of Contract Appeals.

The Supplemental Settlement Agreement dated February 22, 1946, covering the termination of contract W 535 ac-40071, contains the following reservation in Article 4 (c) (2):

> Claim by the Contractor against the Government, as to which his right of reimbursement is disputed, which is excluded without prejudice to the rights of either party, to wit, claim for experimental and development and research costs in the amount of $400,581.44, which is now the subject of an

appeal pending before the War Department Board of Contract Appeals.

At the time the settlement agreement was consummated for contract W 535 ac-20910, there was pending before the War Department Board of Contract Appeals the plaintiff's claim for reimbursement of costs for $274,939.01. The difference of $1,190,123.94 had been reimbursed to the plaintiff, but was recouped by the Finance Officer upon notice of exceptions and suspension by the Comptroller General.

33. On March 27, 1945, the plaintiff executed a renegotiation agreement pursuant to Section 403 of the Sixth Supplemental National Defense Appropriation Act, 1942, as amended, in respect to excessive profits for its fiscal year ending December 31, 1942. This agreement was signed by Colonel Maurice Hirsch, G. S. C., for all services of the United States concerned, and was approved for the Under Secretary of War May 22, 1945.

119 The said agreement covered profits for 1942 on both fixed-price contracts and CPFF contracts with the United States. It provided for refund by the plaintiff of $7,714,000 of excessive profits for the year 1942, after first applying the tax credit applicable to such profits. This agreement provides in part: (See also Finding 17 herein.)

EXHIBIT "C"

* * * * *

PRINCIPLES UNDERLYING SEGREGATION OF SALES AND PROFITS

* * * * *

Allocation of Cost of Sales and Expenses

1. *Cost of sales*:

* * * * *

(g) Deferred Experimental Development, and Production Tooling Expenses in the amount of $1,353,913 were amortized over all planes delivered under Fixed Price Contracts during the year. For the purpose of computing the additional refund under Paragraph VIII of the Agreement, the adjusted amortization chargeable to 1942 of $638,683 was allocated on the basis of the total number of planes delivered under all contracts, both Fixed Price and CPFF.

* * * * *

VIII. In arriving at the refund herein the items of Deferred Experimental Development, and Production Tooling Expenses

in the amount of $728,885.22 have been charged as Costs against Renegotiable Fixed Price Contracts for said fiscal year. The Contractor, in order to conform its method of handling these items to the method adopted by the Bureau of Internal Revenue, has adjusted its figures for said fiscal year by amortizing these items over the total number of planes of the Airacobra type produced, or to be produced, on both Fixed Price and CPFF Contracts (Production Tooling limited to P-39 Models). Such method of amortization and the corresponding reallocation of costs to CPFF Contracts, as well as Fixed Price Contracts, has been tentatively approved by the Army Air Forces, and if the amount allocated to the CPFF Contracts is finally approved by both the Army Air Forces and the General Accounting Office of the Comptroller General of the United States, and reimbursement therefor, is made, the Contractor agrees to pay to the United States as an additional refund the sum of $667,000, on account of which the Contractor shall
120 receive credit for Federal Income and Excess Profits Taxes thereon as determined by the Bureau of Internal Revenue as provided in Paragraph VII hereof.

34. The amortization allowance of experimental, development and the production tooling to fixed-price contracts only, under the foregoing settlement agreement was contrary to the allocations by the Bureau of Internal Revenue, which amortized these costs upon production for all contracts.

By reallocating $2,286,819.95 of the $3,374,465.00 of deferred expense to the CPFF contracts, plaintiff's income from its fixed-price contracts was increased by such amount and the Bureau of Internal Revenue made additional assessments against plaintiff's resulting net income for 1941 and 1942 in the approximate sum of $1,337,474.89. The amount of $2,286,819.95 which the Bureau had disallowed as a cost deduction from the fixed-price contract income in 1941 and 1942, was allowed as a deduction from plaintiff's net income for the years 1943, 1944, and 1945 as costs of performing its CPFF contracts, making plaintiff's taxes for those years approximately $1,305,418.72 less than they would have been had such cost deductions not been allowed or had the $2,286,819.95 been reimbursed by the Air Forces as allowable costs under the CPFF contracts.

It is plaintiff's position that the $2,286,819.95 allowed by the Bureau as a cost deduction from CPFF income for 1943, 1944, and 1945, was in fact a reimbursable item of cost under those contracts. Had plaintiff received reimbursements of the $2,286,819.95 under its CPFF contracts, its net income for tax purposes for the years

1943, 1944, and 1945, would have been greater by that amount and it would have had to pay an additional $1,305,418.72 in taxes, but it would have saved $981,401.23, the difference between the $2,286,819.95 reimbursed, and the $1,305,418.72 which plaintiff would have paid in additional taxes.

VALUE OF EXPERIMENTAL AND DEVELOPMENT WORK TO COST-PLUS-FIXED-FEE CONTRACTS

35. Experimental and development costs capitalized and deferred by the plaintiff for allocation to future production were not segregated as between specific experimental contracts to which
121 they might apply. It was impossible to make any reasonably correct segregation of such costs, since the improvements in design and fabrication developed in the earlier operations were carried forward and applied on later experimental and development work, and finally into production contracts. These costs represent deferred values of designing and experience in fabrication rather than costs of any particular airplane contract.

The plaintiff took over the plant on Elmwood Avenue, Buffalo, New York, in the fall of 1935, which had been vacated by Consolidated Aircraft Company upon its transfer to California, and an abundance of experienced personnel who elected to remain in Buffalo.

The plaintiff's first work involved the installation of an Allison model engine in the nose of a Consolidated airplane. It was the first installation of this kind for the Allison model, which was a heavy 1,000 h. p. engine, whereas other models previously used were normally about 600 h. p. models. It required investigation of the strength of the wings, tail, fuselage and landing gear. The plaintiff's next job was subcontract work for manufacturing all-metal, aluminum, riveted wings for Consolidated flying boats.

The first experimental plane was the XFM-1 Airacuda contracted for May 12, 1936. It was substantially completed by the end of 1937. All costs of experimental and development work on the above projects were charged against these contracts currently or to the plaintiff's profit and loss account, up to and including December 31, 1937. The plaintiff continued further development work on the XFM-1 model in 1938, and later on a contract for service test models of the same type.

36. Some of the basic principles of design and fabrication, which the plaintiff developed on experimental contract work and incorporated into the P-39 production models, include the following:

(a) The installation and successful operation of a liquid-cooled Allison engine, involving installation problems and other features of design necessary to operations.

(b) The extension of the drive shaft, so that the propellers could operate more distant from the engine.

122 This feature was designed on the XFM-1, where the engine was housed in the wing structure, and the pusher-type propellers operated from the rear of the wings. The extension drive shaft was adopted in the P-39, by locating the engine in the fuselage to the rear of the pilot, with the extended drive shaft projected beneath the pilot and operating the propeller in the nose of the aircraft, thereby providing vision for the pilot and permitting the projecting nose of the plane to better accommodate the front wheel of the tricycle landing gear.

(c) The design and successfal installation of air intake ducts for cooling the engine and oil systems, known as "ducted radiator", whereby an intake opening was provided in the leading edge of the wing for admitting air at high velocity.

The air then expanded into larger internal ducts slowing down its velocity for cooling purposes. The overhead air scoop was subsequently incorporated in all P-39's and P-63 planes. The intake was provided on top of these planes, instead of the front edge of the wing, but serving the same purpose of obtaining a simple duct system of air intake to the carburetor of the engine.

(d) The development and installation of a successful anti-shimmy dampening device for the nose wheel of the tricycle landing gear.

The nose wheel of this type of gear was provided with a swivel stirrup to steer the plane on the ground. The nose-wheel shimmy or oscillation was inherent in this type of gear, as the plane would take the runway at high speed or over rough roads. The first successful development of the shimmy dampening device was in connection with the XP-39, although the basic characteristics in this device were developed by the plaintiff in connection with the development and installation of a shock-absorbing gun mount for the XFM-1 plane.

(e) The successful installation of a 37mm. repeating cannon in the XFM-1.

In the flexible gun mountings for the Airacudas the plaintiff devised means of holding and supporting the gun so that it could be properly aimed and provided for the recoil in this type

123 mounting. In the P-39's it was installed in a fixed mounting, but other features of feeding and ejecting the heavy empty cartridges were retained. Provision was made for retaining in the plane the empty shells that were ejected from the cannon, to avoid fouling or damage to the plane when they were

ejected. In lieu of clips, which required manual changing, the plaintiff devised an automatic feed belt to carry the shells into firing position.

(f) Flush riveting, which was developed in the earliest experimental planes, was carried into all later production.

A high-strength aluminum alloy was specified for the XFM-1 fighter plane built by the plaintiff under its first experimental contract. In order to take advantage of the higher structural tensility of this material the plaintiff, by a process of heat treating, sunk the rivets approximately flush with the surface of the metal, which resulted in a smoother external surface in this type of fabrication.

(g) In the construction of the XFL-1 Airabonita, the plaintiff designed and provided very heavy-duty landing gear to accommodate, without undue hazard, the catapult, deck landing and arresting equipment. This tougher type of landing gear was subsequently provided for P-39 models using the tricycle landing gear.

In connection with the XFL-1 for the Navy, the plaintiff also developed a nose-over beam, which extended in the fuselage above and behind the pilot for his protection in case the plane turned over. This feature was also incorporated in the production models of P-39 Airocobras.

(h) Engineering standards which were prepared for experimental work, consisting of short-cut repeat operations, tables and curves of technical information.

Once computed, these standards could be applied thereafter without recalculations.

(i) The earlier Allison engines furnished the plaintiff attained their greatest power at sea level.

In order to give them more power at high altitudes, the plaintiff installed General Electric turbo superchargers which were operated from the engines. Later Allison engines incorporated features to provide power at high altitudes, which duplicated the external unit and voided its further use.

124 (j) The plaintiff also developed and provided compartments in the wing structure of the experimental planes for carrying additional fuel, known as integral fuel tanks.

They were designed to be liquid tight and were enclosed by integral parts of the plane structure, such as the inside beams, bulkhead and outside sheeting. This feature was installed in P-39 models but it was not satisfactorily perfected because of difficulty

with leakage, and was later superseded with bullet-proof storage tanks, by fitting the compartments with rubber and composition cells that would self seal any bullet penetration.

With the exception of the last two features above, the developments, engineering standards and fabricating processes acquired during the manufacture of experimental airplanes were incorporated and utilized on all production. The measure of value to production after 1940 is represented by the plaintiff's excess of costs on experimental airplanes over and above its recoveries under these contracts in the net amount of $1,499,739.23.

37. The plaintiff obtained a basic patent on its development of a hydraulic shimmy-dampening device in the steering mechanism of the nose wheel of the tricycle landing gear, and certain other patents for semi-automatic counter sinkers, twisted spar mills, routers and stake drills. It recovered substantial royalty payments for use of these devices by another manufacturer. As a result of proceedings before a Royalty Adjustment Board, the plaintiff was required to pay over to the Government some $691,666.24, under an indemnity agreement with the War and Navy Departments, representing all royalties collected by it.

There was included in the sums paid over one amount of $102,050.28, which the plaintiff had previously taken into its income and paid taxes thereon. The tax rate during the war years averaged approximately 70 percent of the plaintiff's total net income. No part of the royalties collected was retained by the plaintiff.

The Government also received credit of $360,000 on a contract for an improved model of the P-39, pursuant to an agreement with the plaintiff dated April 11, 1940, which authorized the plaintiff to make certain deliveries to the British of the P-39
125 model airplanes in advance of deliveries under one of the production contracts for the Army Air Corps.

38. After having amortized the total amount of experimental development and production tooling expenses against its fixed-price production contracts, the plaintiff realized a net profit, before taxes and renegotiation of excess profits, of $18,280,732.50.

39. The plaintiff's net income on its fixed-price production contracts, after renegotiation and taxes, was approximately $4,637,607.63.

40. The sum of $1,499,739.23, which was capitalized and deferred by the plaintiff for allocation to future production, represented a fair and reasonable value of the general experimental

and development work in benefits and savings on production contracts.

VALUE OF PRODUCTION TOOLING TO COST-PLUS-FIXED-FEE CONTRACTS

41. Production tooling for the P-39 model was provided during 1939 and 1940. At the end of 1940, the plaintiff capitalized and deferred for allocation to future operations, production tooling costs totaling $1,874,725.77.

This production tooling was used for the fabrication and assembly of airplanes under all of the fixed-price production contracts. Some of the tools other than assembly fixtures became worn out through use or became obsolete on account of current changes from time to time during production.

The major portion of tooling for the P-39 models was used throughout the production of this type of plane under the CPFF contracts. Where replacements or reworking of tools became necessary, the costs were charged against current operations, so that when production under CPFF contracts was commenced the value of prodution tooling was substantially the same as when it was originally installed for use on fixed-price contracts.

In April 1944, the P-39 model was discontinued, and retooling became necessary for the production of P-63 models. All tooling which could not be used in the production of the later model was scrapped and replaced upon approval of the defendant's plant clearance officer.

126 Lists of tools and equipment which could no longer be used on the new models were prepared by the plaintiff, and allocated to certain of the CPFF contracts then in process. The proceeds of the sale of these tools and fixtures were credited to the defendant on CPFF contracts.

The beneficial value of production tooling for P-39 model airplanes manufactured under CPFF contracts was at least equivalent to the beneficial use of such tooling to performance under the fixed-price production contracts.

42. In submitting bids for its fixed-price contracts the plaintiff also submitted data of estimated costs of performing these contracts, the details of which are appended to copies of these contracts. None of the estimates for performing the fixed-price contracts contain any provision for the amortization of experimental, development and production tooling costs.

Estimated costs in the cost-plus-fixed-fee contracts, as specified in Article 2 thereof, were based upon data on file in the office of the Chief of Air Corps, no details of which were attached to these contracts. There is no evidence that these data contained any

estimate for the experimental, development and production tooling costs involved herein.

Article 3 (a) of the CPFF contracts provided for a fixed fee to the plaintiff of 6 percent of the estimated costs under the first two of these contracts and 4 percent of the estimated costs under the last two thereof. This Article contains the additional provision:

> • • • This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article 5 hereof; provided, however, that there shall be no adjustment in the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation, because of any errors and/or omissions made in computing the original estimated cost or where the estimated cost varies from the actual cost.

The provisions for allowable costs are contained in the same article.

The plaintiff reamortized its deferred costs for experimental, development and production tooling expense over all production contracts, as follows:

127

	Fixed-price contracts (Findings 13 and 24)	CPFF contracts (Finding 29)
Experimental and development expense	$463,820.50	$1,035,918.73
Production tooling expense	623,824.55	1,250,901.22
	1,087,645.05	2,286,819.95

The amortization of $1,087,645.05 represents 1.52 percent of the total $71,364,004.86 value of fixed-price contracts, all of which were completed. The amortization of $2,286,819.95 on CPFF contract production represents .71 percent of the total estimated cost plus the fixed fees specified in these contracts. Deliveries called for under CPFF contracts were not completed and the contracts were terminated upon cessation of hostilities August 14, 1945.

Plaintiff's experimental, development, and production tooling costs were properly deferred as intangible capital assets and were properly chargeable as costs of any future production of products for the purpose of which such costs were originally incurred. The amortization of these intangible assets was ratably applied to the total number of P-39 airplanes produced, in accordance with a reasonably consistent plan.

CONCLUSION OF LAW

Upon the foregoing special findings of fact which are made a part of the judgment herein, the Court concludes as a matter of law that plaintiff is entitled to recover $2,286,819.95. It is therefore adjudged and ordered that plaintiff recover of and from the United States the sum of two million two hundred eighty-six thousand eight hundred nineteen dollars and ninety-five cents ($2,286,819.95).

OPINION

HOWELL, *Judge*, delivered the opinion of the court:

Plaintiff sues to recover $2,286,819.95 alleged to be reimbursable items of cost incurred in the performance of four cost-plus-a-fixed-fee contracts (hereinafter referred to as CPFF contracts) for the manufacture and delivery of military aircraft known as P-39's or Airacobras, entered into with defendant through the United States Army Air Corps.[1]

128 Of the total sum claimed to be due under the contracts, $1,035,918.73 represent experimental and development expense, and $1,250,901.22 represent production tooling cost.[2] It is plaintiff's contention that the sum in suit represents allowable costs which should have been reimbursed pursuant to all four CPFF contracts which provide in pertinent part as follows:

> ARTICLE 3 (b). For the purpose of determining the amount payable under this contract, allowable items of cost will be determined by the Contracting Officer in accordance with regulations for determination of the cost of performing a contract as promulgated by the Treasury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940. * * *
>
> ARTICLE 6—*Payments.*
>
> (a) *Reimbursement for Cost.* The Government will currently reimburse the Contractor for such expenditures made in accordance with Article 3 hereof as may be approved or ratified by the Contracting Officer and upon certification to and verification by the Contracting Officer of the original signed payrolls for labor, the original paid invoices for materials or other original papers; * * *

[1] Pertinent details concerning these four contracts are set forth in Finding No. 18.

[2] Finding No. 29.

Pertinent portions of T. D. 5000, referred to in Article 3 (b) are as follows:

SEC. 26.9. *Cost of performing a contract or subcontract*—(a) *General rule.*—The cost of performing a particular contract or subcontract shall be the sum of (1) the direct costs, including therein expenditures for materials, direct labor and direct expenses, incurred by the contracting party in performing the contract or subcontract, and (2) the proper proportion of any indirect costs (including therein a reasonable proportion of management expenses) incident to and necessary for the performance of the contract or subcontract.

* * * * *

(c) *Factory cost.*

* * * * *

(5) *Indirect factory expenses.*—Items usually termed "factory overhead," which are not directly chargeable to the factory cost of performing the contract or subcontract but
129 which are properly incident to and necessary for the performance of the contract or subcontract and consist of the following:

* * * * *

(D) *Fixed charges and obsolescence.*—Recurring charges with respect to property used for manufacturing purposes of the contract or subcontract, such as premiums for fire and elevator insurance, property taxes, rentals and allowances for depreciation of such property, including maintenance and depreciation of reasonable standby equipment; and depreciation and obsolescence of special equipment and facilities necessarily acquired primarily for the performance of the contract or subcontract, except special additional equipment and facilities with respect to which the Secretary of the Department concerned has made a certification binding upon the Commissioner of Internal Revenue, pursuant to section 4 of the Act, in the case of such contract or subcontract. * * *

* * * * *

(d) *Other manufacturing cost.*—Other manufacturing cost as used in paragraph (b) of this section includes items of manufacturing costs which are not properly or satisfactorily chargeable to factory costs (see paragraph (c) of this section) but which upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract or subcontract, as for instance, payments of royalties

and amortization of the cost of designs purchased and patent rights over their useful life; and "deferred" or "unliquidated" experimental and development charges. For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract. In the case of general experimental and development expense which may be charged off currently, a reasonable portion thereof may be allocated to the cost of performing the contract or subcontract. If a special experimental or development project is carried on in pursuance of a contract, or in anticipation of a contract which is later entered into, and the expense is not treated as a part of general experimental and development expense or is not otherwise allowed as a cost of performing the contract, there clearly appearing no reasonable prospect of an additional contract for the type of article involved, the entire cost of such project
130 may be allowed as a part of the cost of performing the contract.

Most of the experimental and development costs herein were incurred by plaintiff in the performance of certain fixed-price experimental contracts entered into with defendant in 1936, 1937, and 1938, for the construction of experimental and service test airplanes known as the "Airacuda", the "Airacobra" and the "Airabonita". (Findings Nos. 3, 4 and 5.) Subsequent to deliveries under these contracts, plaintiff incurred additional expense for further development and improvement of the design of the Airacuda (Finding No. 6). In the case of each experimental contract, the contract price agreed to and paid by defendant represented only a portion of the cost to plaintiff of performance. These excess costs and the later costs of further developing and improving the designs, were capitalized by plaintiff as deferred charges in 1938, 1939, and 1940 for later distribution as an element of cost against future production of the type of plane to which the experiments related.

Plaintiff's auditors allocated the deferred experimental and development costs to the three types of planes, and after deducting a sum disallowed by defendant's Army Audit Agency, there remained in the deferred account $1,499,739.23 (Finding No. 6). Plaintiff received no production contracts for Airacudas or Airabonitas, but it did receive many contracts for the Airacobra or P-39 pursuit fighter plane.

Plaintiff's production tooling costs involved in this suit were incurred first in April 1939, in connection with the performance of its contract with defendant for the production of thirteen service test models of the Airacobra (P-39). Production tooling is restricted in use to specific models or types of the product manufactured and is not as permanent and universal in character as are ordinary machine tools. Production tooling for the Airacobra or P-39 pursuit fighter plane was largely assembly tooling, consisting of long-beam assembly, subassembly and tail-assembly fixtures, all of which were fabricated in structural steel and remained in use as long as this type of plane was in production. It also included metal tubes, angles, form blocks, jigs, router templets and templet dies. In the earlier production of the experi-
131 mental models, most of these fixtures had been fabricated in wood and the tooling was for temporary use only. In the production of the service planes, plaintiff was required to provide for interchangeability of certain parts, such as wings, tails, and surface landing gear, necessitating accurate duplications of the various parts. Subsequent to the April 1939 contract, plaintiff received from the defendant additional fixed-price production contracts for Airacobras during 1939 and 1940 (Finding No. 9) and accordingly plaintiff increased its number of assemblies to provide for greater production, and duplicated the tooling for such assemblies, subassemblies, and such auxiliary tooling as became necessary to meet the increased production requirements.

During 1939 and 1940, plaintiff incurred costs for production tooling for the P-39 Airacobra in the sum of $1,894,109.57 and in December 1940, plaintiff recorded this sum in the deferred account along with the deferred costs of the experimental and development work. This account was entitled "Experimental, Development, and Production Tooling Expenses." Defendant's Army Audit Agency disallowed $19,383.80 of the deferred tooling costs so recorded, leaving in the account $1,874,725.77 for allocation to future production (Finding No. 10).

In connection with the several fixed-price production contracts for P-39's entered into by plaintiff and defendant in 1939 and 1940, plaintiff was required to submit breakdowns of its estimated costs of production. At the time of the contract negotiations, only a portion of plaintiff's experimental and development costs had been determined and set up in the deferred account. Likewise, the production tooling expense involved herein had not yet been determined and set up in the deferred account inasmuch as that expense grew largely out of plaintiff's performance of those fixed-price contracts. Accordingly, the cost estimates submitted in connection with each of plaintiff's fixed-fee contracts in 1939 and 1940 did

not contain any provision for the amortization of any part of the deferred experimental, development, and production tooling costs.

132 As of December 31, 1940, plaintiff had capitalized and deferred its experimental, development, and production tooling expense as follows (Finding No. 13):

Experimental and development expense	*$1,499,729.23
Production tooling for P-39's	*1,874,725.77
Total	*3,374,465.00

* (These are the amounts approved by the Army Audit Agency, referred to above.)

Plaintiff first planned to amortize its deferred experimental, development, and production tooling expenses on the basis of the total number of planes delivered and to be delivered on all contracts on hand at the end of each year, and by prorating such costs annually against deliveries made during the current year (Finding No. 14). Under this plan, the amount of amortization applicable to each airplane produced and delivered would decrease from year to year in proportion to the total increase in the number of planes under contract at the end of each year. At the end of 1940, plaintiff had contracted to deliver approximately 1,600 airplanes under fixed-price contracts, and in 1941 plaintiff received an additional fixed-price contract for 180 planes and parts. In the latter part of 1941 plaintiff and defendant entered into the first two CPFF contracts for 2,392 airplanes of a type similar to those produced and delivered under the aforementioned fixed-price contracts.

Plaintiff's officials were not certain that the deferred experimental, development and production tooling expense would be approved for reimbursement under their CPFF contracts as allowable costs. Accordingly, in order to avoid any question of the reimbursability of such items, plaintiff abandoned its original plan of amortization of these expenses over *all* related production and decided to amortize such deferred expense to the airplanes produced and delivered under the fixed-price contracts only (including the fixed-price contract entered into in 1941) (Findings Nos. 15 and 16). By the end of 1942, plaintiff had amortized the entire amount carried in its deferred account against deliveries of airplanes under its fixed-price contracts (Finding No. 17).

Commencing on August 14, 1941, plaintiff entered into a series of cost-plus-a-fixed-fee contracts with defendants for the
133 production of P-39 (Airacobra) airplanes.[3] One contract was ultimately completed, one was terminated, and two were

[3] Data concerning the dates, quantities, estimated costs and specified fixed fees, are contained in a table in Finding No. 18.

terminated for the convenience of the Government on August 14, 1945, with termination settlement agreements consummated pursuant to the Contract Settlement Act of 1944 (Finding No. 18).

As stated above, by the end of 1942 plaintiff had allocated all of its deferred experimental and production tooling expenses to production under its fixed-price contracts although the items being produced under the CPFF contracts bore as close a relation to such deferred expenses as did the items produced under the fixed-price contracts. In 1942 the Bureau of Internal Revenue of the Treasury Department insisted that for income tax purposes, the deferred expenses in question should have been allocated to planes produced under the CPFF contracts as well as to planes produced under the fixed-price contracts, and, despite plaintiff's protests, the Bureau adjusted plaintiff's income for 1941 and 1942 for amortization purposes by reallocating such expenses to deliveries made under both types of contracts, and allowing as a cost deduction, only a portion of the deferred expense. This reallocation increased the amount of plaintiff's taxable income for these years, and additional taxes were assessed and paid for those years in the approximate amount of $1,337,474.89 (Finding No. 34).

In 1943, Major Knox B. Phagan organized defendant's contract renegotiation activities in the Eastern District Air Forces. Such activities were handled by the Price Adjustment Section of which Major Phagan was Chief. In 1943, the renegotiation of plaintiff's profits on its fixed-price contracts came before that Section. It was the purpose of that Section to make a fair determination of a war contractor's profits in order to determine whether or not such profits were excessive and should be paid back to the Government under the Renegotiation Act of 1942 (56 Stat. 245, 50 USCA § 1191). Major Phagan testified that his attention had been called to the action of the Bureau of Internal Revenue in disallowing the allocation by plaintiff of *all* of its deferred experimental,
134 development, and production tooling expenses to production under its fixed-price contracts, and stated that in general it was the policy of the Price Adjustment Section to follow the decisions of the Bureau of Internal Revenue in such matters for the purposes of renegotiation. Accordingly, the Price Adjustment Section took the position that plaintiff's allocation of all its deferred experimental, development, and production tooling expense to its fixed-price production alone, improperly reduced plaintiff's actual profits on such fixed-price contracts, and that such expenses should have been amortized over production under the cost-plus as well as the fixed-price contracts. Compliance with the position of the Price Adjustment Section, would have resulted in defendant's recouping much larger sums as excessive profits on plaintiff's 1942 income.

On September 7, 1943, plaintiff, by its Comptroller, wrote to the Price Adjustment Board, War Department, setting forth the facts concerning its treatment of the expenses in the deferred account, and stating that Bell was prepared to change its method of amortizing such deferred expense to conform to the views expressed by the Bureau of Internal Revenue and the Price Adjustment Board on condition that the proportion of the deferred expense disallowed by the Board and the Bureau on the ground that it was properly allocable to CPFF production, should become items of reimbursable costs under Bell's CPFF contracts and be allowed and reimbursed as such by the Contract Audit Section of the Army Air Forces and the General Accounting Office (Finding No. 23). On receipt of plaintiff's letter, Major Phagan caused the following statement to be placed on a copy of the letter which he then signed and returned to plaintiff:

> The explanation and method of amortization set forth in this letter is in accordance with our understanding and has our approval.

On September 9, 1943, in accordance with the views of the Bureau of Internal Revenue and the Price Adjustment Board, plaintiff restored to its deferred account the proportion of experimental, development, and production tooling expense which it had been agreed were applicable to airplanes delivered and to be de-
135 livered under plaintiff's CPFF contracts, as follows:

Experimental and development costs	$1,035,918.73
Production tooling for P-39 planes	1,250,901.22

The unrestored difference of $1,087,645.05 previously amortized, represented that portion of experimental, development and production tooling expense which was properly applicable to deliveries under plaintiff's fixed-price contracts in accordance with the approved plan of reamortization.

Plaintiff then prepared and submitted for the approval of the Contracting Officer, reimbursement vouchers in the sum of $451,179.96 representing the reallocation of its amortization of experimental, development, and production tooling deferred expense to deliveries under its CPFF contracts during 1942, and vouchers in the sum of $848,676.06 applicable to deliveries under it CPFF contracts during the period from January to August, inclusive, of 1943 (Finding No. 24). Defendant's Assistant Resident Auditor, Mr. DiLapo, considered the vouchers and recommended to the Resident Auditor, Mr. Campbell, that they be rejected as not constituting costs allowable under the contract for the following reasons: that in the period prior to the inception of the CPFF contracts, the contractor had followed a consistent policy of charging off all of these experimental, development, and production tooling ex-

penses against its fixed-price contracts which were then in effect; that in the opinion of the assistant auditor there was no provision in the CPFF contracts for the reimbursement to a contractor of *losses* suffered under fixed-price contracts (referring to Bell's prior fixed-price experimental contracts in 1936-1938). It would appear that Mr. DiLapo had in mind Section 26.9 (g) (4) of T. D. 5000 which provided in part as follows:

> Among the items which shall not be included as a part of the cost of performing a contract or subcontract or considered in determining such costs, are the following: * * * losses on the other contracts: * * *

Mr. Campbell, the Resident Auditor, did not agree with this position and certified the vouchers to the Contracting Officer, Mr. Bancroft Mitchell. The Contracting Officer approved the vouchers for reimbursement under the CPFF contracts and plaintiff was
136 paid the sums shown thereon, totalling $1,299,856.02, by defendant's Finance Officer.

Commencing in October 1943, plaintiff submitted additional reimbursement vouchers for experimental, development and production tooling expenses representing the proportionate amounts applicable to deliveries subsequent to August 1943 under its CPFF contracts. These vouchers, in the amount of $986,963.93 (Finding 24), represented all the remaining experimental, development and production tooling expense in the deferred account and applicable, under the reamortization plan, to CPFF production. At the time these vouchers began to arrive for audit in October 1943, defendant's Resident Auditor, Mr. Campbell, had been replaced by Mr. Ferris, and the Contracting Officer had been replaced by Captain Davies. Mr. DiLapo was still assistant auditor and he again urged that the expenses represented by the vouchers were not allowable items of cost under the CPFF contracts and should not be paid. His reasons were the same ones previously urged upon Mr. Campbell, and were apparently concurred in by his new superior as well as by a succeeding Resident Auditor, Mr. Leibman. At any rate, the auditors withheld certification of these vouchers.

In April and May of 1944, the Chief Cost Auditor for the General Accounting Office, Buffalo area, submitted to the Resident Auditor a series of "informal inquiries" relative to the previous payment of vouchers covering the $1,299,856.02 of experimental, development and production tooling expense. The General Accounting Officer excepted to such prior payments on the ground that because the deferred expenses had originally been amortized against fixed-price production contracts, "the status of the account [presumably the deferred account] at the time of the negotiations with respect to the estimated costs under his [the contractor's] contract

was such as to preclude consideration thereof as an existing 'Deferred' or 'Unliquidated' charge to the contract" (Finding No. 27). Following formal notices of exception and suspensions of the accounts of Col. Harris, the Finance Officer, issued by the Comptroller General of the United States in August 1944, the Finance Officer recouped the $1,299,856.02 previously paid to plain-
137 tiff by withholding from plaintiff sums totaling that amount which were otherwise due plaintiff.

In the meantime, plaintiff's last series of vouchers, submitted in 1943, and covering the balance of its experimental, development, and production tooling expense in the amount of $986,963.93 had not been acted on by the Contracting Officer. On January 10, 1945, Captain Davies, as Contracting Officer, rendered findings of fact and a decision on these vouchers adverse to plaintiff. On March 1, 1945, Captain Davies rescinded his prior decision and forwarded new findings of fact and a decision (Finding No. 30). The two documents were substantially the same and both concluded that the items of expense covered by the vouchers were not allowable costs under the CPFF contracts and would not be reimbursed. Pertinent details of these two decisions will be discussed hereinafter.

On March 27, 1945, plaintiff appealed the findings and decision of the Contracting Officer to the War Department Board of Contract Appeals and on April 29, 1946, that Board rendered its decision in which it denied plaintiff reimbursement of the sum of $986,963.93. Plaintiff's application for a rehearing was denied by the Board on May 31, 1946.

We shall first consider defendant's administrative defenses. These defenses are, (1) that plaintiff failed to exhaust the administrative remedies provided for in its contracts with respect to the $1,299,856.02 of its claim which was originally paid to plaintiff and later recouped by defendant from money otherwise due plaintiff, and (2) that the decision of the Board of Contract Appeals, adverse to plaintiff with respect to its right to reimbursement for the balance of its claim ($986,963.93), was final and binding on the parties and therefore not reviewable by this court.

Alleged failure of plaintiff to exhaust its administration remedies

Plaintiff's claim falls in two parts for the purpose of defendant's administrative defenses. That part which is the target of the above defense is the $1,299,856.02, representing a por-
138 tion of the experimental, development, and production tooling expense carried in the deferred account and allocated, under plaintiff's revised books, to production of items under the CPFF contracts. Vouchers covering this amount were recom-

mended for approval by defendant's Resident Auditor, approved by the first Contracting Officer, and paid by defendant's Finance Officer in 1943. Subsequently, the General Accounting Office came to the conclusion that the CPFF contracts did not authorize the allowance of such expenses as costs of performing the CPFF contracts, and the Comptroller General suspended the accounts of the Finance Officer who had made the payments to plaintiff. The Finance Officer immediately recouped the amount suspended by withholding from plaintiff an equivalent sum otherwise admittedly due plaintiff. Plaintiff has taken no steps to secure a reversal of the last action of the Finance Officer or to recover the amount withheld other than by bringing this action in court.

It is plaintiff's position that no administrative remedies were provided by its CPFF contracts against the recoupment; that the action of the first Contracting Officer in determining, under Article 3 (b) of its contracts that the amounts shown on the vouchers were allowable costs, was conclusive; that the decision of the Comptroller General, and that portion of the decision and findings of second Contracting Officer in March 1945, which purported to pass on the propriety of the action of the first Contracting Officer, were without effect; that no dispute ever arose under the Disputes article of the contracts concerning this matter and that plaintiff's only remedy lay in the Court.

Defendant's position is that Article 3 (b) of the CPFF contracts merely vests the Contracting Officer with *discretion* to determine allowable costs; that the approval of the vouchers by the first Contracting Officer under that article was purely *routine* and not conclusive nor binding upon the Government; that in any event a dispute did arise involving the sum covered by these vouchers and the recoupment of that sum, which was decided adversely to plaintiff under the Disputes article of the CPFF contracts by the second Contracting Officer in a decision dated March 1, 1945; that plaintiff did not appeal to the Head
139 of the Department from that portion of the findings and decision relating to such previously approved and paid vouchers, and that accordingly plaintiff has no standing in court with respect to that portion of its claim.

We cannot agree with defendant's contention that Article 3 (b) of plaintiff's CPFF contracts merely vested the Contracting Officer with discretion to determine allowable items of cost under T. D. 5000. That article does not say that the Contracting Officer *may* determine allowable items of cost in accordance with T. D. 5000. It says that the Contracting Officer *will* so determine the allowable items of cost. The contract article dealing with "payments" (Finding No. 20) provides that the Government *will cur-*

reatly reimburse the contractor for such expenditures made in accordance with Article 3 as may be approved or ratified by the Contracting Officer. These articles, we think, imposed upon the Government the duties of determining whether costs were allowable under T. D. 5000 and of approving them for reimbursement if they were.

We next turn to the effect of the determination made by the first Contracting Officer under Article 3 (b) that the $1,299,856.02 of experimental, development and production tooling costs evidenced by the vouchers, were allowable items of cost under T. D. 5000. First, we think that a determination made by a Contracting Officer under that Article, followed by actual payment to plaintiff, is conclusive and binding on the parties unless the contractor, being dissatisfied with the decision, makes an objection to it which would result in a dispute to be resolved by the means provided in the Disputes article of the contract. In the case of *James Stewart & Co.* v. *United States*, 71 C. Cls. 126, certain vouchers had been approved by the Contracting Officer under a CPFF contract between plaintiff and the Government, and the amounts shown on the vouchers were paid by the disbursing officers of the Government. The General Accounting Office, deeming the action of the Contracting Officer in approving the vouchers to have been erroneous, made certain disallowances to the amount of such vouchers in the accounts of the disbursing officers.

The Government then sought to recoup such amounts from
140 the contractor by means of a counter-claim against a judgment rendered by this Court in plaintiff's favor in another matter. The Contracting Officer had approved the payment of the vouchers under an article of the CPFF contract which provided in part as follows:

> *Cost of the work.* The contractor shall be reimbursed in the manner hereinafter described for such of its actual net expenditures in the performance of said work as may be approved or ratified by the contracting officer * * *.

The Government contended that the approval of the Contracting Officer under such article was not conclusive, and that upon a showing by the Government that the Contracting Officer was in any respect wrong in making his decision, the Government might recover. The court held that the decision of the Contracting Officer under the above quoted article of the contract was conclusive and was binding on the Government. *Judge Green*, speaking for the court, said, *inter alia:*

> If the decision of the contracting officer as shown by his approval or ratification was not final, his act in so doing was

merely an idle gesture, for the contention of defendant is that notwithstanding such approval it can raise any objection to these items that it sees fit. We do not think the contract can properly be so construed. In fact to so construe it would have the effect to strike from the contract the words "as may be approved or ratified by the contracting officer," for they become absolutely useless. * * * The actions of the parties * * * show very plainly that both parties considered that, subject to other provisions in the contract having no bearing on this particular case, the decision made by the contracting officer was final, and such would be the ordinary meaning given to the provision under consideration. It should also be noted in this connection that there is neither allegation nor proof of fraud, bad faith, or palpable disregard of the rights of either party by the contracting officer. So far as it appears from the evidence, he exercised the authority given him with an honest purpose to carry out the intention of the parties to the contract and his action was an exercise of the power conferred upon him by that instrument. He discharged that duty by the mutual assent of both parties. The terms by which the power was conferred and the duty imposed are clear and precise and they are susceptible of no other interpretation than that the action of the contracting officer in the matter of expenditures was
141 intended to be conclusive, in the absence of fraud, such gross mistake as would necessarily imply bad faith, or a failure to exercise an honest judgment. (pp. 129, 130).

In the instant case the Government does not claim that the record fails to show that the act of approval of the first Contracting Officer constituted gross mistake, or that his approval was secured by fraud on the part of the contractor. In its characterization of the approval as "routine", the Government does seem to imply that the Contracting Officer failed to exercise honest and independent judgment, but the record in the case does not sustain such a characterization. When these vouchers were presented for approval, the Contracting Officer first sought the advice and recommendation of the Resident Auditor and his staff. An assistant resident auditor was of the opinion that the expenses sought to be reimbursed as costs allowable under the contract, were in reality losses suffered by plaintiff on prior fixed-price experimental contracts and that the CPFF contract specifically provided against the allowability of such expenses as costs. This opinion was not concurred in by the Resident Auditor who recommended to the Contracting Officer that the vouchers contained

items properly allowable as costs under the contract. The Contracting Officer agreed with the opinion of the Resident Auditor and approved the vouchers for payment. This set of facts does not, we think, indicate a routine approval of the payment of such a large amount by the Contracting Officer, but rather an independent and honest exercise of his judgment. We accordingly conclude that the first Contracting Officer's decision under Article 3 (b) of the contracts approving the vouchers for payment, was in the circumstances of this case, conclusive and binding on the Government.

The action of the Comptroller General in suspending the accounts of the Finance Officer who had made the payments on the vouchers approved by the first Contracting Officer, and its opinion that the items covered by those vouchers were not allowable items of cost under the contract, did not have the effect of reversing the decision of the first Contracting Officer. As the Supreme Court said in *United States* v. *Mason & Hanger Company*, 260 U. S. 323:

142 Over the effect of these [decisions of the Contracting Officer] the Comptroller of the Treasury has no power. They were the acts and duty of the officer in charge, in the expression of which there was no ambiguity, and were, therefore, conclusive in effect (p. 326).

Next, we come to defendant's contention that a dispute under Article 16 of the contract arose which involved not only the unpaid vouchers for the balance of the deferred expense, but also involved the propriety of the first Contracting Officer's approval of the earlier vouchers, and also the matter of the Government's recoupment of the amount paid to plaintiff pursuant to those vouchers. The defendant says that the second Contracting Officer rendered findings of fact and a decision adverse to plaintiff, and that plaintiff, having failed to appeal to the Head of the Department from that portion of the decision relating to the decision of the first Contracting Officer and the recoupment, has failed to exhaust its administrative remedies under the contract and now has no standing in court as to those matters.

The findings of fact and decision of the second Contracting Officer, dated March 1, 1945, to which defendant refers, did purport to pass on the allowability as costs of the deferred expenses represented by the vouchers previously approved by the first Contracting Officer and paid to plaintiff by the Finance Officer, and also on the matter of the recoupment of a similar amount pursuant to the decision and suspension action of the General Accounting Office. Actually, we think, the only matter before the second Contracting Officer for decision on March 1, 1945, was the

allowability under the contract and T. D. 5000 of items of expense contained in a series of vouchers totaling $986,963.93, representing the balance remaining in Bell's deferred experimental, development, and production tooling account, and which had been allocated by Bell to production under the CPFF contracts. These vouchers began to arrive for audit in October 1943 but none of them were officially acted on until March 1, 1945. At about the time of the first presentation for audit of these particular vouchers, a new Contracting Officer had replaced the officer who had approved the previous series of vouchers, and a new resident auditor was also present on the job. The assistant resident
143 auditor who had recommended disallowance of the first series of vouchers, again made the same recommendation with respect to the second series, and his recommendation was ultimately accepted by the new resident auditor and the new Contracting Officer. In the summer of 1944, following informal inquiries initiated by the General Accounting Office into the payment of the first series of vouchers, and after the suspension of the accounts of the Finance Officer of a sum equal to the amount which had been paid to plaintiff under those vouchers, the Finance Officer recouped the amount suspended by withholding an equivalent amount from money otherwise due plaintiff. At that time, the second Contracting Officer still had taken no final action on the second series of vouchers. Apparently, on December 10, 1943, the resident auditor on the Bell job had written to the District Auditor, Eastern Procurement District, under a subject heading "Amortization of Losses on Fixed Price Contracts," and covering Bell's treatment of the entire amount of experimental, development, and production tooling expenses carried in the deferred account. On January 20, 1944, the Eastern Procurement District forwarded the letter of December 10, 1943, and all subsequent correspondence on the matter, to the Chief of the Procurement Division for his views "as to the right of Bell to be reimbursed under its CPFF contracts for any portion of the said amount." On November 13, 1944, the Chief of the Procurement Division wrote to the District Supervisor of the Eastern Procurement District reviewing in general the facts concerning the deferred account and Bell's handling of the account, and expressing the opinion that the amount of such expense which Bell had allocated to the CPFF contracts did not, in fact, represent costs of performing such contracts, and concluding as follows:

> It is therefore the opinion of this Headquarters that Bell is not entitled to reimbursement under its CPFF contracts for P-39 and P-63 airplanes for any portion of the said sum of $2,286,819.95.

The sum so mentioned included both the amount covered by the vouchers approved by the first Contracting Officer and paid to plaintiff, and the amount covered by the second series of vouchers which were before the second Contracting Officer for approval.

144 On January 10, 1945, the second Contracting Officer wrote to plaintiff stating that he was forwarding a copy of the above-mentioned decision of the Chief of Procurement on the reimbursement of amortization of development and experimental expense over CPFF contracts, and that the Contracting Officer was incorporating that decision as his findings of fact "in denying reimbursement to the contractor for this expenditure, as requested on Audit Bureau Vouchers as follows:". The Contracting Officer then listed the unpaid vouchers totaling $986,963.93. On March 1, 1945, the Contracting Officer wrote to plaintiff again stating that the findings of fact and the decision which he had rendered on January 10, 1945, were rescinded and new findings and a decision were being forwarded. The new findings began with a listing of the identical unpaid vouchers, and continued almost word for word in the same manner as previously, except for the omission of the first paragraph of the prior findings which had related to the circumstances under which the Chief of Procurement Division was rendering advice, and a change in the last sentence of the "findings" to make it read, "It is, therefor, the decision of the Contracting Officer" rather than "It is therefore the opinion of this Headquarters."

The November 13, 1944, letter from the Chief of Procurement, was merely an expression of the views of that office on the question of the reimbursability of deferred experimental, development, and production tooling costs under plaintiff's CPFF contracts. That letter discussed the problem generally and referred to the entire amount in the deferred account and to the vouchers previously approved and paid, as well as to the subsequent series of vouchers which were before the Contracting Officer for approval. The Contracting Officer, for some reason, adopted this letter (as pointed out above) as his findings of fact and decision, but since the only matter actually before the Contracting Officer for decision was the approval or disapproval of the second series of vouchers, the findings and decision of the Contracting Officer are without any effect on plaintiff insofar as they related to vouchers other than the second series actually before him. In its subsequent and timely appeal from this decision to the Board of Contract Appeals for the War Department, plain-

145 tiff referred only to the second series of vouchers which had been disapproved, and the Board confined its decision to the matter of the disallowance of those particular vouchers.

In our opinion, plaintiff was not obliged by its contract to take an appeal from that portion of the second Contracting Officer's decision which purported to pass on the matter of the prior approval of the first series of vouchers, or on the matter of the recoupment. The decision of the first Contracting Officer had been favorable to plaintiff and no dispute arose over his decision which called into play the provisions of the Disputes article. Further, there was no occasion for the second Contracting Officer to make any findings or render any decision with respect to such prior decision of the first Contracting Officer. Plaintiff had nothing to appeal from with respect to the decision of the first Contracting Officer and the contracts afford the Government no right of appeal from that decision. The Government's only recourse, if it disagreed with such a decision, was to effect recoupment if possible, and, in the event of a lawsuit, attempt to show that because of some vital circumstance, the decision of the first Contracting Officer had been robbed of its usual conclusiveness.

The subsequent recoupment of an amount equal to that covered by the first vouchers which had been approved and paid, was not a matter which plaintiff was bound to appeal to the head of the department under any provision of its contract. If anything, it was a matter which plaintiff might consider a breach of the Government's contractual undertaking to pay sums admittedly due, and was the proper subject of a lawsuit.

We conclude that plaintiff has not failed to exhaust its administrative remedies with respect to the first series of vouchers or the recoupment of the amount paid under such vouchers. Furthermore, inasmuch as the defendant has failed to point to any circumstance which would defeat the conclusiveness of the decision of the first Contracting Officer, and since the General Accounting Office was without the power to reverse such decision, plaintiff is entitled to recover the amount approved for payment, paid and subsequently recouped, in the sum of $1,299,856.02.

146 *Finality of the decision of the War Department Board of Contract Appeals*

That portion of the second Contracting Officer's findings and decision of March 1, 1945, which dealt with the allowability as costs of $986,963.93 of deferred experimental, development, and production tooling expense, was duly appealed by plaintiff to the War Department Board of Contract Appeals and that Board decided that such items of expense were not reimbursable under plaintiff's CPFF contracts.

Defendant says that pursuant to the Disputes articles in the CPFF contracts, the decision of the Board was final and that no appeal therefrom lies in the courts. The Disputes article appearing in each of the contracts is the usual one in the standard form of Government contracts, and provides that, except as otherwise specifically provided in the contract, all disputes concerning questions of *fact* arising under the contract, not disposed of by mutual agreement, shall be decided by the Contracting Officer in writing; that such decision may be appealed by the contractor within 30 days to the Secretary of War or his designated representatives, whose decision thereon shall be final and conclusive upon the parties thereto (Finding No. 20).

It is plaintiff's position that the decision of the War Department Board of Contract Appeals is not binding on this Court because the Board's conclusion concerned a question of law and not of fact, but that if the Court should consider the question to be one of fact, then the Board's conclusion is not binding because it is arbitrary and capricious and directly in conflict with its own primary findings of fact.

Defendant contends that the question in dispute and decided by the Board was one of fact and not one of law. Defendant points out that the Contracting Officer had found as a fact that the sum in question "which plaintiff had charged on its books against CPFF contracts does not, in fact, represent costs of performing such CPFF contracts." Defendant urges that by dismissing plaintiff's appeal, the Board was, in effect, sustaining that finding of fact.

In its decision the Board set forth the facts concerning plaintiff's deferred account and its fixed-price and CPFF
147 contracts, much as we have done in our findings of fact herein. The Board stated that there was no dispute between the parties as to the amount of the costs involved, nor as to the propriety of the plaintiff's method of allocation; that the CPFF contracts provided that allowable items of cost were to be determined by the Contracting Officer in accordance with the pertinent provisions of T. D. 5000; that the experimental and development costs in question were clearly within the category of indirect costs as defined by T. D. 5000 and were specifically covered by Section 26.9 (d) thereof; that the production tooling covered by the deferred production tooling costs were used in the performance of the CPFF contracts; that such items of cost were within the intent and meaning of T. D. 5000, specifically, Section 26.9 (e) (5) (D) (Finding No. 31). The Board then stated, however:

> Although it is true that costs of this type may properly be allowed as reimbursable items under T. D. 5000, it does not follow that such costs *must* be reimbursed under T. D. 5000 in all cases and *under all circumstances*. In order to determine whether such items of costs should be reimbursed it is necessary to examine all of the circumstances and facts involved. [Italics supplied.]

The Board then referred to the fact that plaintiff had originally planned to amortize all such expense over a fixed-price contracts only; that after entering into the CPFF contracts, plaintiff had changed its plan of amortization in accordance with the position taken by the Bureau of Internal Revenue and the Renegotiation authorities, and had revised its books to spread the amortization over *all* its contracts for production of the P-39 airplane, both fixed-price, and cost-plus. The Board concluded as follows:

> Under these circumstances, it is difficult to understand how it can now be reasonably contended that an item of cost is reimbursable under the terms of the subject contracts, when, at the time the contracts were negotiated appellant did not intend that the item should be reimbursable and was in fact charging the costs in question against other contracts in accordance with a previously adopted plan. * * * Under the circumstances here present, the Board is of the opinion that the costs are not reimbursable under the subject contracts.

148 In making the above statement, we think the Board had reference to the language in T. D. 5000, Sec. 26.9 (d) which states that "upon a complete showing of all pertinent facts [these costs] are properly to be included as a cost of performing the contract * * *." Accordingly, the Board held that the circumstance of plaintiff's not having originlly intended to allocate any portion of such costs to the CPFF contracts was one of the circumstances contemplated by the contract (T. D. 5000) as foreclosing reimbursement of this type of cost, otherwise reimbursable. This was not, we think, a conclusion that the items in question were not "costs of performing such CPFF contracts." Without going into the merits of whether this was the sort of circumstance or "pertinent fact" contemplated by Section 26.9 (d) of T. D. 5090, we think that the Board's decision on whether, under the circumstances here present, the contract required reimbursement, involved an interpretation of plaintiff's CPFF contracts. That the Board itself so viewed its decision is indicated by the following language in its decision:

> There is no dispute between the parties as to the amount of the costs or as to the propriety of the method of allocation used by appellant. The only question presented is whether reimbursement for any portion of these costs is authorized or required by the subject contracts under the circumstances here involved.

In the case of *Wunderlich* v. *United States*, 117 C. Cls. 92, we pointed out that the distinction between questions of law and questions of fact is not always a clear one, but that in general the courts have held that questions of the interpretation of contracts are not "questions of fact" within the meaning of that expression as it is written into the Disputes articles of Government contracts. *McWilliams Dredging Company* v. *United States*, No. 48894, decided June 5, 1950, and cases cited therein. In its decision in the *Bell* case, the Board of Contract Appeals noted that the contracts all contained the standard "Disputes" article which referred only to decisions on questions of fact. The Board then stated:

> Insofar as the questions presented by this appeal are questions of law they will be administratively determined pursuant to the memorandum of the Secretary of War dated 4 July 1944.

149 That Memorandum gave the Board the following power, *inter alia:*

> (b) Consider and administratively pass on appeals not specifically or impliedly authorized by the contract where the ruling appealed from is not thereby made final and conclusive, and the appeal is taken within the time fixed in the contract for appeals.

The appeal in this case to the Board was from a decision of the second Contracting Officer that the items of expense involved were not allowable items of cost of performing the CPFF contracts, and also from his decision that such items were accordingly not reimbursable under the contracts. In his decision, the Contracting Officer made no reference to Article 3 of the contracts nor to T. D. 5000. In reviewing this decision, the Board carefully analyzed both the contract and T. D. 5000 and made findings not previously made by the Contracting Officer. The Board then concluded that the phraseology of the contract and T. D. 5000 made the items in question allowable items of cost,[4] but that certain circumstances, not

[4] To that extent the Board's ruling appears to be contrary to the ruling of the Contracting Officer.

specified in the contract or in T. D. 5000, but which, in the opinion of the Board, were contemplated therein, constituted a bar to reimbursement.

The decision of the Contracting Officer that the CPFF contracts did not permit reimbursement of these items was an interpretation of the contract and thus did not involve a question "of fact." The contracts themselves did not specifically nor impliedly authorize an appeal from such a decision, nor did the contracts make such a decision final and conclusive. In reviewing such a decision of the Contracting Officer, and in rendering its decision, the Board of Contract Appeals was only exercising the power defined in the Memorandum of the Secretary of War to consider and administratively pass on an appeal of this sort. Nothing in that Memorandum nor in the contracts, made the Board's decision on that question binding on plaintiff so as to preclude an appeal therefrom to the court. The Board might well have refused to exercise its discretion to render a decision in this case. In *Appeal of*
150 *Quipco Associates, Inc.*, (ASBCA No. 841, July 30, 1951), the Board had the following to say:

> The question as to what in fact was the subject matter of the contract of sale presents an issue which can be resolved only by a proper construction of the contract as a whole. Whether the contract, properly construed, contemplated identification of the subject matter of the sale by any words of description contained in the contract, or contemplated identification in some other manner such as by seller's display of the materials offered for sale, and whether or not Appellant is now entitled to any relief, including rescission, on the basis of the facts alleged, concerns essentially questions of law. * * * Any relief to which Appellant may be entitled could be granted only on the basis of a determination that as a matter of law the quoted provisions [of the contract], despite its phraseology, does not bar the granting of such relief. In that respect, also the dispute does not lie within the scope of the disputes clause * * * which is limited to disputes concerning questions of fact.

In some cases the Board has, as in the instant case, exercised its discretion to administratively pass on a "question of law." In the *Appeal of Nash-Kelvinator Corporation* (NBCA 289, April 24, 1947) and in the *Appeal of Consolidated Vultee Aircraft Corporation* (NBCA 524, February 28, 1949) the Navy Board of Contract Appeals had before it questions similar to the one in suit, i.e., whether under CPFF contracts the contractor was entitled to reimbursement as allowable costs, of a properly allocated portion of certain contributions made to local charitable organizations. The Board in each case stated that it was considering the appeal

pursuant to its directive from the Secretary of the Navy, which directive gave the Board *discretion* to consider and administratively pass on questions involving interpretations of contracts. In both cases the Board held that the contracts, properly interpreted, entitled the contractors to reimbursement for the contributions in question. In the *Consolidated Vultee* case, the contracting agency acquiesced in the Board's decision and requested payment be made to the contractor. The General Accounting Office, however, refused to permit payment and the contractor brought suit in the District Court (*Consolidated Vultee Aircraft Corporation* v.
151 *United States,* 97 F. Supp. 948). It is interesting to note that in the District Court proceeding, the Government's principal defense was that the Navy Board of Contract Appeals had no jurisdiction to decide *finally* whether an item of alleged cost was reimbursable under the CPFF contract because, under the Disputes article of the CPFF contract, its jurisdiction was confined to deciding questions of fact, whereas the question to be decided involved the interpretation of the contract, and, as such, was not a question of fact. The District Court did not pass on whether the question involved was one of fact or otherwise, and we mention the case only because in the instant controversy, involving an almost identical question, the Government is contending that the question is one of fact.

There is no doubt in our minds that the question decided by the War Department Board of Contract Appeals in the *Bell* case involved the interpretation of the CPFF contracts and the question was therefore not one of fact. Accordingly, an adverse decision of that Board did not bar plaintiff from bringing an appeal therefrom to this Court.

We now turn to the parties' position concerning the merits of the controversy on the law and on the facts.

Defendant says that the deferred experimental and development expenses are not properly allowable costs because in reality they were losses suffered by plaintiff in the performance of its fixed-price experimental contracts in 1936, 1937 and 1938 and that their reimbursement is specifically forbidden by Section 26.9 (g) (4) of T. D. 5000 which reads in part as follows:

> * * * Among the items which shall not be included as a part of the cost of performing a contract or subcontract or considered in determining such cost, are the following: * * * losses on other contracts; * * *

It is true that the bulk of the expenses in question contained in the deferred account were incurred in the performance of the experimental contracts with the Government, although a portion of them were incurred by plaintiff in the course of further research

after completion of the experimental contracts. It is also true that the contract price agreed to and paid by defendant on each experimental contract was much less than the actual cost to plain-
152 tiff of performance.

In the performance of a *production* contract, if the cost of performing exceeds the sale price of the articles produced, such excess costs certainly represent a loss since the purpose of a production contract is to realize an amount in excess of all costs of production. However, in the performance of an experimental contract, the failure to realize therefrom an amount over and above the costs of performance does not necessarily result in a loss. Experimental and development costs are similar to organization expense or preliminary work in connection with any project or contract, the benefits of which will inure to an indefinite period or later operations. The benefit of such costs may well apply to later production, the extent of which might be indefinite or possibly unknown at the time the costs are incurred. Business prudence however, would preclude the deferment of any costs of this nature unless the management had reasonable grounds for believing that it would receive contracts or other business against which such costs might properly be amortized. Where there is reasonable expectation that the research and experimentation carried on in the performance of an experimental contract will be used in future production contracts, the costs in excess of the contract price paid for such experimental work are properly to be deferred and carried in the contractor's financial statement as intangible assets (sometimes referred to as temporary capital assets), although they may represent substantial costs incurred for designs, formulae, patterns and engineering tables having great value in the production of the type of product for which such designs and calculations were prepared. If the project for which such experimental and development expenses were incurred were completely abandoned and an entirely new venture pursued, then these deferred costs would be determined to have no inherent value or benefit to later production and would be charged off to the company's surplus account
153 even though a deficit would result.[5] However, where the company secured production contracts for items directly related to the experimental work, the deferred intangible assets are usually and properly amortized and written off against such production so that the financial statement of the company will be void of items of an indeterminable value. The period of amortization may be indefinite and will depend largely upon the prospects

[5] In the instant case, for example, if plaintiff had diverted its attentions and efforts to the production of ships, tanks or automobiles to which its experimental and development work would have no application, it would have been improper for plaintiff to have deferred such costs for application against later production.

of volume production which would benefit by the deferred costs previously incurred.

In plaintiff's case, the demand for fighter planes was greater than production capacity. As early as 1938 plaintiff was reasonably sure that future production contracts would result from its experimental work on the fighter planes, and it commenced to defer its experimental and development expense. The war in Europe started in September 1939 and during that year plaintiff received its first production contract (a fixed-price contract) for approximately 87 P-39 fighter planes. At the end of 1939 and the end of 1940 plaintiff deferred additional costs which it incurred in the course of further experimental and development work for this type of plane. Other production contracts for the plane were received in 1940 which assured increased production of this type of plane.

In view of the continuity of the demand and the war engagements of the United States, it was reasonable and proper for plaintiff to extend the period of amortization against performance of production contracts which it received from time to time after 1940. Since the production contracts contained adequate provisions for compensation in case of termination for the convenience of the Government, it was also proper to include the total number of planes specified in such contracts as a basis for prorating the amortization of the experimental and development costs. Plaintiff could, within the limits of any possible corporate charter restrictions, have amortized these intangible capital assets over part or all of the production contracts directly related to the experimental work which created the assets. Inasmuch as all the items produced under the contracts were so related, it was the best practice to carry out the amortization over all such contracts since such experimental expenses were truly an element of the cost of producing each item called for by such contracts.

154 The terms "costs" and "losses" are not synonymous, and in the case of experimental projects which lead to profitable production contracts, the excess of costs of the experimental work over the price paid for such work, represents a temporary or intangible capital asset and not a loss. In plaintiff's case, the experimental and development work which it had done led to its receiving very large production contracts, and the products so manufactured embodied benefits which derived from the prior experimental work. Therefore the costs incurred in the latter would in no sense be considered losses, notwithstanding the fact that the actual costs of the experimental work were not fully recovered under the experimental contracts.

We accordingly conclude that the prohibition against inclusion as costs of performance in production CPFF contracts of losses

sustained on other contracts (T. D. 6000, Sec. 26.9 (g) (4)) does not apply to these experimental and development costs.

Next, defendant contends that the production tooling expenses carried in the deferred account were not actually a part of the cost of production under the CPFF contracts. Production tooling was commenced in 1939 and increased in volume as plaintiff received additional production contracts during 1940. Although plaintiff had received fixed-price contracts for approximately 1,600 planes by October 1940, only a small portion of deliveries were completed under these contracts by the end of 1940. Accordingly, it was proper for plaintiff to defer the tooling cost for the performance of these contracts and allocate such costs to deliveries in later years.

The CPFF contracts called for the same type of fighter plane for which the tooling had been provided in the performance of the fixed-price contracts. Thus, the tooling provided for the fixed-price contracts was utilized, with replacements from time to time, in the production of the same type of plane under the CPFF contracts. To the extent the performance under the CPFF contracts utilized the original tooling or replacements thereof, the original costs became properly applicable to performance under the CPFF contracts. Part of the original tooling became worn out or
155 obsolete during production on fixed-price contracts and had to be replaced. The cost of replacing tools was charged currently to production on fixed-price contracts, so that when the work was started on the CPFF contracts, the value of the original tooling was substantially the same as its original costs. Then, when these tools were scrapped due to a later change in model, the proceeds of the sale of such tools or scrap was credited entirely to the Government under the CPFF contracts. We conclude that a portion of the production tooling exepnse carried in the deferred account was properly a part of the cost of producing the planes under the CPFF contracts.

Next, the defendant says that if the Court should hold, as we do, that plaintiff's deferred experimental, development, and production tooling costs were actually a valid part of the cost of producing each item under both the fixed-price and the CPFF contracts, plaintiff still cannot recover because the Government did not in fact agree in the CPFF contracts that such costs would be reimbursed. Defendant bases this conclusion on the fact that until 1943 it had been plaintiff's intention to amortize *all* such costs over its fixed-price production contracts only and that plaintiff in fact did so; that it was not until the Bureau of Internal Revenue and the Renegotiation authorities of the Government insisted that such an allocation improperly reduced plaintiff's actual profits on its fixed-price contracts; that plaintiff reallocated such

deferred costs to all production, including production under its CPFF contracts; that these costs were not included in plaintiff's original negotiations for the CPFF contracts, but that they were included in plaintiff's bids on the fixed-price contracts; that reimbursement of this type would be contrary to the intentions of the contracting parties as shown by all the facts.

The intention of the contracting parties may become important and perhaps controlling in the interpretation of a contract where the language of that contract is ambiguous and not clear. In the instant case Article 3 (b) of the CPFF contracts provided that allowable items of cost would be determined by the Contracting Officer in accordance with "Regulations for determination of the cost of performing a Contract as promulgated by the Treas-
156 ury Department in Section 26.9 of Chapter 1 of Title 26 of Code of Federal Regulations, as contained in T. D. 5000 and approved by the Secretary of War August 2, 1940." Section 26.9 (c) (5) (D) quoted both in Finding No. 19 and earlier in this opinion, provides that charges for depreciation of property used in the manufacturing process may be treated as an item of cost. The deferred charges for production tooling clearly fall within this category of factory costs. Section 26.9 (d) also quoted in Finding No. 19 and earlier in this opinion, specifically provides that deferred experimental and development charges "upon a complete showing of all pertinent facts are properly to be included as a cost of performing the contract." There is nothing ambiguous about the language of the contract or T. D. 5000 regarding the treatment the parties agreed would be accorded to the charges in question. It appears to be defendant's position, however, that certain "pertinent facts" present in this case prevent the treatment of these charges as items of cost of performing the contract at least for the purposes of reimbursement.

There is no real dispute between the parties as to the existence of most of the "pertinent facts" relied on by the Government: that the costs were incurred several years prior to the entry into the cost-plus contracts; that in the course of the CPFF negotiations plaintiff had not intended to allocate any of such charges to production under the CPFF contracts and did not include any part of such charges in its costs estimates. What, then, is the significance of those facts on the question of plaintiff's right to reimbursement?

That the expenses were incurred several years prior to the entry into the CPFF contracts is, we think, immaterial, since the charges were incurred and properly deferred in the expectation that the experiments would lead to profitable production contracts for the manufacture and sale of articles to which the research and develop-

ment would apply, and the CPFF contracts in question represented a portion of the fulfillment of that expectation. The production tooling, although used for production under the fixed-price contracts, was also used for the CPFF production and could not be used for producing other types of planes.

157 Plaintiff did not, at the time it was negotiating for the CPFF contract, intend to allocate any of its deferred experimental, development, and production tooling expenses to the CPFF contracts, and in its estimate of costs which it was required to make and present to the Government in negotiating the CPFF contracts, plaintiff did not include any amount to cover costs of this type. The contract itself provides for the consequences of such an omission from a contractor's cost estimates in Article 3 (a) as follows:

> The Government will pay the Contractor upon satisfactory delivery of all items specified in this contract, subject to reimbursements for cost, as outlined in Article * * * hereof, the cost, plus a fixed fee of * * * Dollars and * * * cents * * * being * * * percent * * * of the total estimated cost of * * * Dollars * * *. This estimated cost and the fixed fee are subject to increases or decreases resulting from authorized changes as provided in Article * * * herein, provided, however, that there shall be no adjustment of the amount of the fixed fee as provided herein, nor shall there be any claim for increased compensation because of any errors and/or omissions made in computing the original estimated cost or where the estimated cost varies from the actual cost.

Plaintiff omitted the items of expense in question from its estimated cost upon which its fixed fee was based and that omission would be a complete defense to a claim by plaintiff for an increase in its fixed fee. But plaintiff is not seeking an increase in its fixed fee and nothing in Article 3 indicates that a legitimate item of cost may not be reimbursed merely because it was omitted from the original cost estimates.

The omission of these expenses from cost estimates was intentional on plaintiff's part and was apparently communicated to defendant. However, it has not been shown that defendant relied on plaintiff's intention not to request reimbursement and because of such reliance changed its position so as to work an estoppel. The record merely indicates that some agent of defendant had expressed the opinion to plaintiff, prior to the execution of the CPFF contracts, that experimental, development, and production tooling expenses would not be reimbursable, and that plaintiff accordingly

decided not to request reimbursement. This understanding,
158 if any, was not expressed in the contracts ultimately entered into, although it might easily have been done by expressly excluding such items in the contract. A similar situation existed in the *Appeal of Nash-Kelvinator Corporation*, NBCC 289, a case decided by the Navy Board of Contract Appeals on April 24, 1947. In that case the dispute involved the reimbursability of certain charitable contributions expressly made reimbursable under paragraph 40 (f) of Explanation of Principles for Determination of Costs under Government Contracts, a document relative to costs similar to T. D. 5000, and incorporated by reference into the CPFF contract. On the basis of a departmental expense ruling and a decision of the Comptroller General, the Navy Department denied reimbursement. In holding for the contractor, the Board stated:

> Had it been the intention of the Government to exclude contributions of the character described in paragraph 40 (f) from allowable costs, the obvious means of achieving such exclusion would have been the omission of paragraph 40 (f) and the express exclusion of such expenses.

See also *Todd Shipyards* v. *United States*, (No. 48916) decided by this court on November 7, 1950.

As to defendant's contention that plaintiff had included all these deferred costs in its estimates used in bidding on the fixed-price production contracts, the Commissioner has found (Findings No. 12 and No. 41) and we have adopted his finding, that plaintiff did not include such costs in its bid estimates. At the time plaintiff was bidding on the fixed-price production contracts executed in 1939 and 1940, (Finding No. 9 for dates of execution of those contracts), only a portion of plaintiff's experimental and development costs had been determined and set up in the deferred account, and the production tooling expense involved herein had not yet been determined inasmuch as that expense grew largely out of the performance of those fixed-price production contracts. In any event, we do not believe that the inclusion or exclusion by plaintiff of these costs in its bid estimates would have any bearing on the issues of this case. It is our understanding that in making a bid, a fixed-price contractor usually tries to arrive at a price sufficiently low to secure the award, but high enough to secure a profit. In
159 figuring a bid and in performing the contract, the cost problem as such, is one for the contractor. His contract protects him from increased costs clearly due to changed conditions or changes brought about by Government action, and the Government, in turn is protected from improper allocations of cost by the Renegotiation Act. Regardless of how much of the instant costs were

actually included in the fixed-price bid estimates, plaintiff did attempt to allocate all of these costs when determined, to its fixed-price contracts, whereupon the Government proceeded, under the Renegotiation Act, to protect itself by disallowing a portion of the costs in the computation of plaintiff's profits for renegotiation purposes in 1942.[6]

We conclude that plaintiff's intention not to allocate any part of the costs in question to its CPFF contracts and its omission of such costs from the cost estimates submitted to defendant in negotiating such CPFF contracts, are not "conditions" or "pertinent facts" which makes those costs non-reimbursable under the CPFF contracts. The actual omission is significant only for the purpose of computing plaintiff's fixed fee, and the amount of such fee is not involved herein. The contracts as entered into all expressly provided that such costs would be reimbursed. Plaintiff was under no contractual obligation to request reimbursement for any particular costs, but the contracts did obligate the Government to reimburse plaintiff for any costs made reimbursable by the contracts if, as here, reimbursement was requested.

In its defenses to the merits of plaintiff's claim, defendant makes the same argument urged earlier in the administrative defenses, that the contract and T. D. 5000 made the Contracting Officer's determination of allowable costs merely discretionary. We have already decided that the language of Article 3 (b) imposes upon the Contracting Officer the obligation to determine whether or not costs are allowable under T. D. 5000. The use of the word "may" in the latter part of Section 26.9 (d) of T. D. 5000 does not weaken that obligation as a reading of the whole section will demonstrate.

Defendant also contends that in order that deferred or capitalized experimental and development expenses be reimbursable as
160 costs, they must have been amortized in accordance with a reasonably consistent plan. Defendant urges that plaintiff, in extending the amortization of the costs of experimental work over the production under CPFF contracts instead of confining such amortization to production under its fixed-price contracts as previously planned, had, in fact, two plans of amortization and that these plans were inconsistent. Plaintiff's basic plan of amortization (Finding No. 14) was to amortize these expenses over future production of products utilizing the designs and plans developed and this, in fact, is what plaintiff dd. There was never any change in that basic plan. Both the Board of Contract Appeals and this Court have found that the amounts requested by plaintiff for reim-

[6] The terms of the settlement agreement ultimately entered into by the parties, are discussed elsewhere in this decision.

bursement represented a proper proportion of such deferred expense determined by "a ratable allocation which is reasonable in consideration of the pertinent facts."

Defendant further contends that the charges in question are not allowable items of cost because T. D. 5000 contemplated reimbursement only of "*unliquidated* experimental and development charges." It is defendant's position that these charges were completely liquidated under plaintiff's first plan of amortization against the fixed-price contracts by the end of 1942. Section 26.9 (d) which describes "other manufacturing cost" properly includable as a cost of performing the contract, mentions "deferred" or "unliquidated" experimental and development charges. As an explanation of what is meant, the section states:

> For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract.

At the time plaintiff presented its first vouchers for reimbursement of these charges, plaintiff had completely revised its books back to 1940, so that only that portion of its deferred charges ratably allocable to production under the fixed-price contracts had been amortized. The amount of experimental and develop-
161 ment charges for which reimbursement was requested on the vouchers was still carried in the deferred account and met all the tests of Section 26.9 (d). Neither the Bureau of Internal Revenue nor the Government Renegotiation Authorities considered these deferred charges actually or irrevocably "amortized" or "liquidated" by plaintiff's previous bookkeeping entries which had charged them all off to production under the fixed-price contracts. In their opinion, no amount of bookkeeping could alter the actualities of the situation, i.e., that these deferred charges were properly costs of every plane produced which utilized the designs, experimentation and production tooling represented by such charges. By the time plaintiff submitted its vouchers under the CPFF contracts, it had changed its bookkeeping to reflect the true state of affairs.

Our discussion above relates in part to another contention urged by defendant, namely, that to allow plaintiff to be reimbursed for the deferred charges properly allocable to production under the CPFF contracts, woud in effect be to pay plaintiff twice for the same thing. This "double payment" argument seems to be based on the theory that because plaintiff made a profit on its fixed-price

production contracts sufficient to cover all of the deferred charges, those charges were automatically written off or "liquidated". Plaintiff has pointed out exactly where such an argument could lead. For example, if plaintiff had, in fact, suffered losses on the fixed-price contracts, which losses exceeded in amount the total of the deferred charges, and plaintiff had elected to amortize none of those deferred charges over such fixed-price contracts, then, under defendant's theory, all of the deferred charges would be allowable items of cost reimbursable under the later CPFF contracts, since there had been no profits from the fixed-price contracts to affect the "liquidation" of those charges. It is obvious from the language of Section 26.9 (d) of T. D. 5000 that such an allocation of all deferred charges to a CPFF contract where a portion of them represented the cost of producing items under other contracts, was not contemplated and would not have been permitted. Regardless of profit or loss resulting from production contracts, the deferred charges represented a portion of the cost of every plane produced under such contracts and plaintiff's revised books so treated the deferred charges.

162 Defendant suggests that the Government received nothing of value that it would not have received under the original conditions as they existed at the time the CPFF contracts were negotiated, and that plaintiff incurred no expense that it would not have incurred had no CPFF contracts been made by it with the Government. By the expressin "under the conditions as they existed", defendant apparently is referring to the then state of plaintiff's bookkeeping which had allocated all of the deferred charges to the fixed-price contracts. As we have stated previously, a proper portion of those deferred charges were elements of cost of producing planes under the CPFF contracts regardless of plaintiff's books, and had the experiments not been conducted and the charges not incurred, defendant could not have secured any of the planes from plaintiff. The fact that the expenses were incurred prior to the entry into the CPFF contracts does not prevent a portion of those expenses from being costs of manufacturing planes under those contracts, as T. D. 5000, Section 26.9 (d) expressly provides. As for the deferred production tooling expenses which plaintiff had originally amortized against fixed-price contracts only, plaintiff's bookkeeping and its original intentions regarding amortization do not alter the fact that those production tools were used in producing the CPFF planes and a certain portion of those deferred charges were actually a part of the cost of such production.

Finally, defendant says that if the Court should hold that the deferred charges in question constitute allowable items of cost under the CPFF contracts which should have been reimbursed, then only

the excess costs in the sum of $229,986.30 which had been allocated by plaintiff to the experimental "Airacobra" contract should be charged off against subsequent P-39 production. Defendant urges that plaintiff has not shown that the balance of the deferred experimental and development charges, allocated to the Airacuda and the Airbonita experimental work were of benefit in the P-39 production.

As pointed out in our Finding No. 6, all excess costs on experimental contracts were classified as experimental and development expense and were accumulated from year to year during the performance of the several experimental contracts. No
163 segregation of these costs was made as to their application to the specific contracts on which excess costs were incurred except the first amount deferred in 1938 which resulted from work on the experimental contract for the Airacobra. Plaintiff's auditors made an approximate allocation of this expense to the three experimental contracts by deducting from the costs of fulfilling each contract, the income received, and under that allocation (set out in Finding No. 6) the approximate allocation to the Airacobra was $229,986.30. Actually, no reasonably correct segregation of costs to any particular experimental contract had been possible since the improvements in design and fabrication developed in earlier operations were carried forward and applied on later experimental and development work on other models and finally into production contracts. The costs thus represented deferred values of designing and experience in fabrication rather than costs of any particular experimental airplane contract. In Finding No. 36 there are described some of the basic principles of design and fabrication which plaintiff developed on its experimental contract work and incorporated into the P-39 production models. Most of the developments, engineering standards and fabricating processes acquired during the performance of all three experimental contracts were incorporated and utilized in all subsequent production. The few developments not specifically utilized in the planes produced were of value because of the engineering knowledge gained that the particular design or development was not entirely satisfactory. The Commissioner has found, and we have adopted his finding, that the true measure of the value of the experimental work on all three models to production of planes after 1940 is represented by the excess of costs on the experimental contracts over and above recoveries under these contracts in the net amount of $1,499,739.23, and that sum is thus the fair and reasonable value of the general experimental and development work in benefits and savings on the later production contracts.

Under the clear provisions of plaintiff's CPFF contracts and T. D. 5000, a portion of plaintiff's deferred experimental, develop-

ment, and production tooling expenses were allowable items
164 of cost and should have been reimbursed. The portion sought to be amortized against the CPFF contracts and claimed as allowable costs subject to reimbursement (Finding No. 41) represents a reasonable allocation of such costs on the basis of all production contracts. The sum so allocated is $2,286,819.95 and plaintiff may have judgment for that amount.[7]

It is so ordered.

WHITAKER, *Judge;* and LITTLETON, *Judge;* concur.

JONES, *Chief Judge*, dissenting in part:

I would disallow the second item of $986,963.93.

I agree that the Contracting Officer's decision was not necessarily final.

I would allow plaintiff to recover on the item which was paid and later recouped. This item had been approved by the Contracting Officer. Since it had been paid it manifestly had the approval of the other authorized officers of the Government. In the absence of fraud or mistake this should have been treated as final.

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[7] The matter of plaintiff's taxes and the final renegotiation settlement have been the subject of considerable discussion in this case. Neither matter is directly in issue or has a real bearing on plaintiff's right of recovery. The Bureau of Internal Revenue has already applied plaintiff's costs in the manner plaintiff is contending for herein. However, since these costs were denied as reimbursable costs under the CPFF contracts, the Bureau allowed these costs, on a pro rata basis, as deductions from the net fees that the plaintiff realized on its CPFF contracts for deliveries of planes during 1943, 1944, and 1945 (Finding No. 33). Had these costs been reimbursed by the Government under the CPFF contracts, the Bureau would not have allowed such costs as deductions from the fees collected. Accordingly, plaintiff's recovery of these costs herein will become taxable since they were allowed as deductions during 1943, 1944, and 1945.

The Bureau of Internal Revenue also allocated part of these costs to deliveries in 1942 both on fixed-price and CPFF contracts. But the profits on the fixed-price contracts during 1942 were much greater, and the entire year was subject to renegotiation by the War Department (Finding No. 32). However, the Renegotiation Board calculated plaintiff's profits on the original basis of charges for experimental, development, and production tooling costs amortized against plaintiff's fixed-price contracts only (Finding No. 16), disregarding the revision made by the Bureau of Internal Revenue. The amount of excess profits recouped by the Governmnt was thus less than it would have been if these charges had been allocated to all planes delivered and deliverable under all contracts then in force. Plaintiff was required to refund $7,714,000 on the basis of total and excess profits so determined, but the agreement provided that if the pro rata allocation sought by plaintiff was carried through and allowed on all planes delivered under the CPFF contracts, the 1942 charges for experimental, development, and production tooling expenses against fixed-price contracts would be reduced to the extent of such reallocation, and the excess profits recoverable under the renegotiation would be increased by $667,000 which plaintiff agreed to pay to the Government, less whatever tax credit plaintiff might be entitled to by so refunding to the Government this amount as excessive profits for 1942. The remaining sum would then become subject to further tax. All actual amounts must be calculated by the General Accounting Office in its ultimate settlement with plaintiff and plaintiff's settlement with the Bureau of Internal Revenue.

165 MADDEN, *Judge*, dissenting:

The War Department Board of Contract Appeals in its decision which is quoted in Finding 31 said:

> Under these circumstances, it is difficult to understand how it can now be reasonably contended that an item of cost is reimbursable under the terms of the subject contracts, when, at the time the contracts were negotiated appellant did not intend that the item should be reimbursable * * *.

The essence of this case is contained in the above statement. Is the plaintiff entitled to be paid $2,286,819.95 for something which, when it made the contracts under which it claims the payment, it intended that it should be paid nothing at all?

The plaintiff says that the contract, as written, calls for the payment, and that therefore it is entitled to it even though it did not count upon it or expect to get it, when it made the contracts. To bring about such a result, the contracts would have to speak in the plainest and most unmistakable language. But they did not do so. They spoke the language of T. D. 5000 which is quoted in Finding 19. In its paragraph (d) it says:

> For example, in case experimental and development costs have been properly deferred or capitalized and are amortized in accordance with a reasonably consistent plan, a proper portion of the current charge, determined by a ratable allocation which is reasonable in consideration of the pertinent facts, may be treated as a cost of performing the contract or subcontract.

Before the cost-plus-fixed-fee contracts here in litigation were entered into, the plaintiff was following a method of amortization which would have completely written off these charges without attributing any of them to any future contract. After three of the four cost-plus-fixed-fee contracts were made, on August 14, 1941, September 10, 1941 and June 29, 1942, the plaintiff continued,
166 down to the end of 1942, to pursue the same system of accounting, and by that time had completely amortized all of the costs claimed in this suit. On September 19, 1942, plaintiff's treasurer wrote plaintiff's comptroller that it would be improper accounting to charge any of these expenses against cost-plus-fixed-fee contracts since, to make them reimbursable costs under those contracts, such costs "would have to be included in the original negotiations of such contract. No provision is made for that on any of our cost-plus contracts in view of the position taken by the Government that prior to our entry into cost-plus contracts we have received sufficient fixed-price contracts to permit the

amortization of deferred experimental expenses." See Finding 22.

This statement of course referred to the position taken by the Government at the time the contracts were entered into. It certainly did not refer to the position taken currently by the Bureau of Internal Revenue of the Government, which was exactly the opposite. See Finding 21. And there is nothing in the record tending to indicate that there had been any discussion between the plaintiff and the contracting officers of the Government between the time that the contracts were negotiated and the time of the above-quoted communication, with regard to what should or should not be reimbursable. Finding 15 shows that the plaintiff set up its plan, limiting amortizatoin to its fixed-price contracts because it understood that the charges here in question were not to be reimbursable under its cost-plus-fixed-fee contracts.

The quoted statement of the treasurer puts beyond question the intention of the parties that the costs here sued for were not to be reimbursable. Their recovery is a complete and unexpected windfall of $2,286,819.95.

I have not failed to consider any equity in the plaintiff's favor which might arise from the fact that the change in the plaintiff's accounting method resulted from pressure which the Bureau of Internal Revenue put upon the plaintiff, in the Bureau's desire to establish a larger amount of excess profits made from the plaintiff's fixed-price contracts. As it turned out, the plaintiff's taxes for the years 1941 through 1945, during which it performed both the fixed-price and the cost-plus-fixed-fee contracts,
were increased only $32,056.17 over what they would have
167 been if they had been computed on the basis of the plaintiff's own method of accounting. As to the renegotiation of the plaintiff's contracts, the arrangement made was only tentative, and the plaintiff would not be prejudiced in that regard by an adverse judgment in this case.

The opinion of the Court accords finality to the Contracting Officer's approval of vouchers in the amount of $1,299,856.02, which were, accordingly, paid, and which are here in suit because that amount was subsequently recouped by the Government from amounts admittedly due the plaintiff under its contracts. I think the opinion of the Court is correct in not attributing to the plaintiff any failure to exhaust its administrative remedies in this regard. I think that the contract did not provide any administrative procedure which had to be followed, at the peril of losing a valid claim. But, on the other hand, I think that the provisions of Article 3 (b) of the contract, quoted in Finding 19, that "allowable items of cost will be determined by the Contracting Officer • • • " did not confer upon that officer the powers of an agreed

arbitrator such as are normally conferred upon that officer by Articles 4 and 15 of the usual Government contract. Article 3 (b) says nothing about finality and I would not be willing to decide that a cost-plus-fixed-fee contractor who was entitled to be reimbursed for an expenditure could be irrevocably denied reimbursement because the contracting officer, acting under Article 3 (b), had refused to approve the expenditure for reimbursement because he construed the contract erroneously. If such a question arose, and the contractor was dissatisfied with the amount paid him, I think he would have the right to establish his claim in this or some other competent court, without being prejudiced by an administrative decision which the court thought was wrong. For the same reason I think that the Government was not foreclosed by the erroneous decision of its Contracting Officer. He had no more power to give the plaintiff $1,299,856.02 which it had not contracted for than he would have had to deny the plaintiff that sum if it had been entitled to it under its contract.

I would dismiss the plaintiff's petition.

169 JUDGMENT OF THE COURT, OCT. 2, 1951

Upon the special findings of fact, which are made a part of the judgment herein, the Court concludes as a matter of law that plaintiff is entitled to recover.

IT IS THEREFORE ADJUDGED AND ORDERED that plaintiff recover of and from the United States the sum of two million two hundred eighty-six thousand eight hundred nineteen dollars and ninety-five cents ($2,286,819.95).

[Clerk's Certificate to foregoing transcript omitted in printing.]

17. SUPREME COURT OF THE UNITED STATES

No. ——, October Term, 1951

United States, *Petitioner*,

v.

Bell Aircraft Corporation

Order Extending Time to File Petition for Writ of Certiorari

Upon Consideration of the application of counsel for petitioner,

It Is Ordered that the time for filing petition for writ of certiorari in the above-entitled cause be, and the same is hereby, extended to and including January 30, 1952.

Fred M. Vinson,
Chief Justice of the United States

Dated this 29th
day of December, 1951.

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1951

No. ——

THE UNITED STATES, *Petitioner*,

v.

BELL AIRCRAFT CORPORATION

STIPULATION AS TO PRINTING OF RECORD

Subject to this Court's approval, it is hereby stipulated and agreed by and between the attorneys for the respective parties hereto that for the purposes of petitioning for a writ of certiorari, the printed record shall consist of the pleadings, the findings of fact, conclusion of law, opinions and judgment of the Court of Claims, dissenting opinions by Jones, *Ch. J.*, and by Madden, *J.*, and the docket entries for the Court of Claims subsequent thereto.

It is further stipulated and agreed that the parties hereto may refer to the unprinted portions of the entire record which is being filed with this Court but which are not included in the proposed printed record herein.

PHILIP B. PERLMAN,
Solicitor General

WM. M. AIKEN,
Counsel for Respondent

January 17, 1952

☆ U.S. GOVERNMENT PRINTING OFFICE 1952—986372/P.O. 713

Supreme Court of the United States

No. 559, October Term, 1951

[Title omitted.]

Order allowing certiorari

Filed March 31, 1952

The petition herein for a writ of certiorari to the United States Court of Claims is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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